



April 13, 2018
Office of the Compliance Advisor Ombudsman (CAO)

COMPLIANCE APPRAISAL: SUMMARY OF RESULTS

Axzon-01 (IFC Project #31990)
Ukraine

On May 31, 2013, IFC approved (i) a senior loan of up to EUR36 million to Axzon and (ii) an equity investment of up to DKK134,137,081 (approximately USD23 million) in Axzon A/S holding company. Axzon Group is an agricultural and food production company operating in Denmark, Poland, Ukraine and Russia. This compliance appraisal relates to complaints about the impacts of Danosha Ltd., a subsidiary of Axzon Group (both are hereinafter referred to as “the client”). Danosha is a vertically integrated pork producer from grain cultivation to the sale of live pigs for processing across seven farms in the Ivano-Frankivsk region of western Ukraine. The expansion of the client’s operations in this region was a specific target of IFC’s investment. This appraisal will consider complaints about three Danosha operated farms: Luka, Delievo and Lany.

On February 2, 2014, CAO received a complaint submitted by community members in the Ivano-Frankivsk region, with support from the National Ecological Centre of Ukraine. The complaint alleges violation of IFC Performance Standards 1, 3, 4 and 6, with respect to: (1) environmental and social assessment and management system; (2) air, water and soil pollution; (3) water extraction; (4) Halych National Nature Park; (5) road wear, cracks, dust emission, access and land encroachment; (6) land use and associated compensation; and (7) stakeholder engagement and grievance mechanism.

The purpose of a compliance appraisal is to ensure that compliance investigations are initiated only for those projects that raise substantial concerns regarding environmental and/or social outcomes, and/or issues of systemic importance to IFC/MIGA.

Having considered the issues raised by the complainants and undertaken both a review of available documentation and a site visit, CAO has identified concerns as to IFC’s review and supervision of the project. While having decided to close specific issues in relation to impacts to the Halych National Nature Park, road encroachment, land use, and stakeholder engagement and grievance mechanism, CAO will conduct an investigation of IFC’s E&S performance in relation to the remaining issues. Thus, CAO’s investigation will focus on the adequacy of:

- IFC’s review and supervision of the client’s ESMS, including measures to ensure that procedures are in place to test for, and mitigate against, environmental pollutants;
- IFC’s review of the (i) ESIA documentation (including water extraction, carrying capacity and manure management system) and (ii) associated consultation and disclosure, where relevant;

CAO notes that the decision to initiate a compliance investigation does not imply a finding in relation to the client’s E&S performance adverse or otherwise.

Terms of Reference for this compliance investigation will be issued in accordance with CAO’s Operational Guidelines.

About CAO

The Office of the Compliance Advisor Ombudsman (CAO) is an independent post that reports directly to the President of the World Bank Group. CAO reviews complaints from communities affected by development projects undertaken by the two private sector lending arms of the World Bank Group, the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA). The CAO's mission is to serve as a fair, trusted, and effective independent recourse mechanism and thus to improve the environmental and social performance of IFC and MIGA. CAO consists of three unique and complementary functions, Dispute Resolution, Compliance and Advisory, which together provide a flexible framework for handling people's complaints and addressing systemic concerns about IFC and MIGA projects.

About CAO's Compliance Function

CAO's Compliance function provides oversight of IFC and MIGA investments with the objective of improving environmental and social (E&S) performance of the institutions. The compliance function is activated when either of the parties opt for it following CAO's assessment of the complaint or when the Dispute Resolution process does not lead to an agreement between the parties. The compliance function can also be initiated by the CAO Vice-President, the President of the World Bank Group or IFC/MIGA senior management. Following a compliance investigation, CAO may determine that it is necessary to monitor actions taken by IFC or MIGA until such actions assure CAO that its compliance findings are being addressed.¹

For more information about CAO, please visit www.cao-ombudsman.org.

¹ CAO Operational Guidelines, 2013, para. 4.4.6.

Table of Contents

Acronyms.....	4
I. Overview of the Compliance Appraisal Process.....	5
II. Background.....	6
Investment.....	6
Complaint.....	6
Appraisal methodology.....	7
III. Analysis.....	7
Environmental and Social Assessment and Management System.....	7
Air, Water, and Soil Pollution Prevention.....	10
Water Extraction.....	12
Road-related Impacts.....	13
Land-use and Associated Compensation.....	15
Stakeholder Engagement and Grievance Mechanism.....	15
IV. CAO Decision.....	16

Acronyms

Acronym	Definition
CAO	Office of the Compliance Advisor Ombudsman
DKK	Danish Krone
E&S	Environmental and Social
EBRD	European Bank for Reconstruction and Development
ESAP	Environmental and Social Action Plan
ESIA	Environmental and Social Impact Assessment
ESMS	Environmental and Social Management System
ESRS	Environmental and Social Review Summary
EU	European Union
EUR	Euro
IFC	International Finance Corporation
IPPC	Integrated Pollution Prevention and Control
MIGA	Multilateral Investment Guarantee Agency
PS	Performance Standards
USD	United States Dollar

I. Overview of the Compliance Appraisal Process

When CAO receives a complaint about an IFC or MIGA project, the complaint is referred for assessment. If CAO concludes that the parties are not willing or able to reach a facilitated solution, the case is transferred to the CAO compliance function for appraisal and potential investigation.

A compliance appraisal also can be triggered by the CAO vice president, IFC/MIGA management, or the president of the World Bank Group.

The focus of the CAO compliance function is on IFC and MIGA, not their client. This applies to all IFC's business activities, including the real sector, financial markets and advisory. CAO assesses how IFC/MIGA assured itself/themselves of the performance of its business activity or advice, as well as whether the outcomes of the business activity or advice are consistent with the intent of the relevant policy provisions. In many cases, however, in assessing the performance of the project and IFC's/MIGA's implementation of measures to meet the relevant requirements, it will be necessary for CAO to review the actions of the client and verify outcomes in the field.

In order to decide whether a compliance investigation is warranted, CAO first conducts a compliance appraisal. The purpose of the compliance appraisal process is to ensure that compliance investigations are initiated only for those projects that raise substantial concerns regarding environmental and/or social outcomes, and/or issues of systemic importance to IFC/MIGA.

To guide the compliance appraisal process, CAO applies several basic criteria. These criteria test the value of undertaking a compliance investigation, as CAO seeks to determine whether:

- There is evidence of potentially significant adverse environmental and/or social outcome(s) now, or in the future.
- There are indications that a policy or other appraisal criteria may not have been adhered to or properly applied by IFC/MIGA.
- There is evidence that indicates that IFC's/MIGA's provisions, whether or not complied with, have failed to provide an adequate level of protection.

In conducting the appraisal, CAO will engage with the IFC/MIGA team working with the specific project and other stakeholders to understand which criteria IFC/MIGA used to assure itself/themselves of the performance of the project, how IFC/MIGA assured itself/themselves of compliance with these criteria, how IFC/MIGA assured itself/themselves that these provisions provided an adequate level of protection, and, generally, whether a compliance investigation is the appropriate response. After a compliance appraisal has been completed, CAO can close the case or initiate a compliance investigation of IFC or MIGA.

Once CAO concludes a compliance appraisal, it will advise IFC/MIGA, the World Bank Group President, and the Board in writing. If a compliance appraisal results from a case transferred from CAO's dispute resolution, the complainant will also be advised in writing. A summary of all appraisal results will be made public. If CAO decides to initiate a compliance investigation as a result of the compliance appraisal, CAO will draw up terms of reference for the compliance investigation in accordance with CAO's Operational Guidelines.

II. Background

Investment

Axzon Group is an agricultural and food production company operating in Denmark, Poland, Ukraine and Russia. On May 31, 2013, the Board of Directors of the International Finance Corporation (IFC) approved: (i) a senior loan of up to EUR36 million to Axzon and (ii) an equity investment of up to DKK134,137,081 (approximately USD23 million) in Axzon A/S holding company. The purpose of the investment was to support expansions and acquisitions in Poland, Ukraine and Russia. The loan was fully prepaid in June 2017. Additionally, IFC committed to an A-loan of EUR10 million in August 2016, which was subsequently cancelled in July 2017. However, IFC's equity investment remains active.

The investment is part of a larger financing package with support of the European Bank for Reconstruction and Development (EBRD).

This compliance appraisal relates to complaints about the impacts of Danosha Ltd., a subsidiary of Axzon Group (both are hereinafter referred to as "the client"). Danosha is a vertically integrated pork producer from grain cultivation to the sale of live pigs for processing across seven farms in the Ivano-Frankivsk region of western Ukraine. The expansion of the client's operations in this region was a specific target of IFC's investment. This appraisal will consider complaints about three Danosha operated farms (Luka, Delievo, and Lany).

The client follows a three-stage production cycle comprised of sow, weaner and finisher farms. Manure generated from the swine is stored, handled and applied to cultivated land as fertilizer to produce grains and silage for pig feed. To ensure nutrient balance, nearly one hectare of agricultural area is prescribed per sow in production.²

Complaint

On February 2, 2014, CAO received a complaint from community members in the Ivano-Frankivsk region. The community members are from Sivka-Voynylivska village, in Kalush district, and from Delievo and Lany villages, in Halych district. The complainants raised concerns in relation to three of the client's farms, Luka (in close proximity to Sivka-Voynylivska), and Delievo and Lany farms (located in the villages of the same name). The complainants received support from the National Ecological Centre of Ukraine. At the time of the complaint, Luka and Lany farms were operational while construction of the Delievo farm was ongoing. CAO received a supplement to the complaint dated February 15, 2017, from community members from the same villages with support from the Environment People Law organization. The complaint is accessible on CAO's website.³

CAO determined that the complaint was eligible in March 2014. Following an attempt at dispute resolution, the communities of Kalush and Halych districts formally withdrew from the process in June and July 2016, respectively. The complaint was transferred to the CAO compliance function for appraisal in March 2017.

The complainants allege violation of IFC Performance Standards (PS) 1, 3, 4, and, 6 with respect to: (1) environmental and social assessment and management system; (2) air, water and soil pollution; (3) water extraction; (4) Halych National Nature Park; (5) road wear, cracks, dust emission, access and land encroachment; (6) land use and associated compensation; and (7) stakeholder engagement and grievance mechanism.

² As explained by IFC, approximately one hectare is required per sow in production with all its offspring, from piglets to hogs, at any given time.

³ See http://www.cao-ombudsman.org/cases/case_detail.aspx?id=218.

Appraisal methodology

This compliance appraisal was based on a review of IFC internal documents, public domain project information and discussions with relevant stakeholders. The CAO compliance team discussed the matters raised in the complaint with the IFC project team, complainants and their representatives, the client's management and EBRD's Project Complaint Mechanism. In May 2017, CAO sought the input of an external swine production specialist. The CAO team visited Ukraine in August 2017 and met with the client, IFC staff, community members and the village councils of Sivka-Voynylivska, Delievo and Lany, civil society organizations and national and regional authorities. This appraisal report takes into account the discussions the CAO team had with the various parties.

The CAO compliance team's visit included a two-day tour of Luka, Delievo, and Lany farm facilities and surrounding areas.

During this appraisal, the team sought the views of the client relevant to each of the areas of concern the complainants raised. These views are described in the analysis below.

III. Analysis

The 2013 IFC investment in Axzon was processed under the 2012 Policy and Performance Standards on Environmental and Social Sustainability, and Access to Information Policy, jointly referred to as the Sustainability Framework. It was classified as Category B, as it was considered to have limited potential environmental and social risks and impacts.

This compliance appraisal will consider, in light of the issues raised in the complaint, IFC's environmental and social performance with respect to:

- Performance Standard 1
- Performance Standard 3
- Performance Standard 4
- Performance Standard 6

Environmental and Social Assessment and Management System

The complainants question the adequacy of the environmental and social impact assessment (ESIA) for the client's farms. They argue the project should be categorized as one with significant adverse E&S risks and/or impacts. The complainants allege the farms are operating at a higher density of swine than allowed in the environmental permit. They believe this is increasing air, water, and soil pollution and associated community health and safety risks, without implementation of appropriate mitigation measures. The complainants believe the client is operating in their villages without providing information about environmental and public health-related risks and impacts or mitigation measures despite requests for information. They maintain that there has been limited engagement, public participation in decision-making in matters having direct impacts on their environment and health. They argue that the environmental assessment (including disclosure and associated public consultations) and related permits do not meet Ukrainian legal requirements.

For all prospective projects, IFC is required to carry out environmental and social (E&S) due diligence that is commensurate to the level of environmental and social risks and impacts.⁴ In

⁴ IFC Policy on Environmental and Social Sustainability, January 2012, para. 26.

cases where the business activity is already conceived, “*IFC will review the [prospective client’s] ESMS and risk management practices already in place, as well as the environmental and social assessment client [...] before IFC’s consideration of the investment.*”⁵

Where E&S risks and impacts of the project are identified, the client is required to address them as part of an Environmental and Social Management System (ESMS). IFC may require a corrective action plan to reach full E&S compliance with IFC standards. To this end, if IFC is not satisfied that the Performance Standards can be met “*within a reasonable period of time,*” it commits not to finance the project.⁶

Under PS1 (Assessment and Management of Environmental and Social Risks and Impacts), IFC requires its clients to establish and maintain a process for identifying the environmental and social risks and impacts of the project. The type, scale, and location of the project then informs the scope and level of effort devoted to the risks and impacts identification process. PS1 further requires that the scope of the risks and impacts identification process be consistent with good international industry practice, and will determine the appropriate and relevant methods and assessment tools.⁷ In addition, clients are required to comply with applicable national law.⁸

PS1 stipulates the client’s responsibility to “*provide Affected Communities with access to relevant information on [...] (iii) any risks to and potential impacts on such communities and relevant mitigation measures [...].*”⁹ Further, IFC commits to make publicly available electronic copies or web links to any relevant ESIA documents prepared by or on behalf of the client.¹⁰

Pursuant to PS1, the process of consultation must provide affected communities with relevant information, meaningful opportunities to participate and express views and sufficient time to consider issues.¹¹

Applicable to this investment, the World Bank Group’s Environmental, Health, and Safety Guidelines (EHS) for Mammalian Livestock Production, states that manure may be used as a fertilizer on agricultural land after careful assessment of potential impacts. The results of the assessment may indicate the need to some level of treatment and preparation prior to its application. The EHS Guidelines require the observation of internationally recognized guidance, such as that published by FAO, on land requirements for livestock production for livestock units (LU) per hectare (ha) to ensure an appropriate amount of land for manure deposition.¹²

As part of the pre-investment appraisal, IFC prepared an Environmental and Social Review Summary (ESRS), which was disclosed on February 15, 2013.¹³ The scope of the review, as it relates to the client’s activities, included field visits to selected pig farms in Ukraine as well as potential new acquisitions. The ESRS notes that the “*new farms are based on latest construction principles and are designed and established according to modern EU [European Union] criteria, as a copy of latest farm designs from Denmark, with pesticide, fertilizer, and animal health*

⁵ IFC Policy on Environmental and Social Sustainability, January 2012, para. 27.

⁶ IFC Policy on Environmental and Social Sustainability, January 2012, para. 22.

⁷ IFC Performance Standard 1, January 2012, para. 7.

⁸ IFC Performance Standards Overview, January 2012, para. 5.

⁹ IFC Performance Standard 1, January 2012, para. 29.

¹⁰ IFC Access to Information Policy, January 2012, para. 31.

¹¹ IFC Performance Standard 1, January 2012, para. 30.

¹² World Bank Group Environmental, Health, and Safety Guidelines for Mammalian Livestock Production, April 30, 2017 page 3.

¹³ IFC Environmental and Social Review Summary, February 2013, <https://disclosures.ifc.org/#/projectDetail/ESRS/31990>.

principles transferred accordingly.” CAO recognizes the client’s technical expertise in swine breeding, crops growing, and in the overall operation of pig farming.

Relevant to the complainants’ concerns, the ESRS states that “*the new greenfield farms are developed after the preparation of local ESIA Studies, while older farms are going through the approval procedures for existing operations.*” The ESRS adds that for all farms, procedures will be “*in line with the EU IPPC Directive [...]. These norms are similar to, but typically more stringent than the IFC Performance Standards requirements.*”¹⁴ The ESRS also references the appointment of environmental and health & safety officers who prepare operational procedures for environmental management and occupational health and safety. IFC described the E&S management system as “*well functioning [...] validated during appraisal.*” While noting that “*farms do not carry large scale risks.*”

An Environmental and Social Action Plan (ESAP) for the client was disclosed on the IFC website,¹⁵ with express requirements to:

- prepare emergency management system policies harmonized for corporate level (Axzon) application to be translated and adopted by country-level operations;
- deliver corporate-level terms of reference for environmental officers and E&S performance management person(s), including duties and reporting lines;
- ensure pesticide and fertilizer usage are used in accordance with local legislation, including enforcement of non-application zones around drainage and water channels;
- include liquid effluent control in case of manure spills in all future design specifications
- maintain balance between animal hold, manure production/composition and farmed crop land
- prepare and disclose formalized emergency preparedness and response plan

IFC maintains that at time of investment, permits for Delievo farm had been granted and the ESIA amended (2013) to reflect project design updates. While acknowledging consultations associated with the ESIA were limited, IFC indicates the disclosure requirements were fulfilled by the client, in accordance with national law. The process, as related by IFC, included public hearings and disclosure of information for a specified period of thirty days, during which time no complaints were submitted.

IFC notes the client’s semi-annual village council meetings, annual door-to-door questionnaire, notice boards, social fund, annual mobile visiting center, and public education tours. The client recognizes the wealth of information it possesses, the importance of its disclosure and expresses its intention to release a non-financial report covering both social and environmental issues on its website. It notes that information with respect to manure application and potential intensified-related odor is posted on bulletin boards three to seven days prior to application.

During the CAO compliance site visit, meetings with various government bodies revealed a complex legislative and institutional landscape. In this context, CAO notes that Ukraine’s environmental management framework is subject to ongoing decentralization and reform, creating challenges relevant to environmental regulations. As documented by the World Bank, this includes, a lack of continuity between central and local governments and an evolving ESIA system which has limited consultation and disclosure requirements.¹⁶

¹⁴ The Integrated Pollution Prevention and Control (IPPC) Directive is a set of common rules for minimizing pollution from various industrial sources throughout the European Union.

¹⁵ IFC, Environmental and Social Action Plan, Project #31990, available at: <https://disclosures.ifc.org/#/projectDetail/ESRS/31990>.

¹⁶ World Bank Ukraine Country Environmental Analysis, January 2016, available at:

CAO notes the client conducted an ESIA as required by IFC.¹⁷ However, CAO notes that the ESIA document is currently unavailable on neither IFC's nor the client's website. IFC informed CAO that, at the time of the investment, the ESIA document was disclosed on the client's website for a period of 30 days as required by national law at that time. The client has, however, made a non-technical summary of the ESIA available through its website.¹⁸ Given legislative complexities, it remains unclear to CAO whether ESIA disclosure and consultation were aligned with requirements of relevant national legislation and IFC requirements. In relation to IFC, it is unclear as to why the ESIA document is not available through the IFC website, as required by the AIP.¹⁹

Regarding IFC's environmental review and monitoring, CAO notes a discrepancy between required stocking density (number of pigs) stated in the ESIA and that in reviewed operational data. This raises questions about the number of pigs permitted at the Delievo farm the corresponding manure output and manure storage (lagoon capacity), processing, and application. In this context, CAO has questions regarding IFC's pre-investment review of relevant environmental documentation and ongoing monitoring with respect to the concerns set out above. Finally, CAO has questions as to the adequacy of IFC's pre-investment review of the client's ESMS.

Air, Water, and Soil Pollution Prevention

The complainants raise concerns about the impacts of air pollution and strong odors on the health and well-being of the public. They allege that air emissions at Luka farm exceed permissible levels ten-fold and is subject to ongoing judicial consideration. They also raise concerns about the potential contamination of ground and surface waters by over-application of manure or because of leakages from pipelines. The complainants cite manure leakages in 2015 in Delievo village, linking it to excessive concentrations of ammonia in water sources. They fear contamination of Burkach stream, Dniester River and ground water may threaten their sources of drinking water. Further, they are concerned that over-application of manure will result in reduction in soil fertility and land value.

PS3 (Resource Efficiency and Pollution Prevention) states that a client should “*consider ambient conditions and apply technically and financially feasible [...] pollution prevention principles and techniques that are best suited to avoid, or where avoidance is not possible, minimize adverse impacts on human health and the environment.*” It adds that the principles and techniques applied during the project life-cycle will be tailored to the hazards and risks associated with the nature of the project and consistent with good international industry practice (GIIP).²⁰ This applies to air, water, and soil pollutants, of a routine, non-routine and accidental nature.

PS4 (Community Health, Safety, and Security) recognizes that project activities can have unintended adverse impacts on community health and safety that need to be evaluated. The client is required to “*establish preventive and control measures consistent with good international industry practice.*”²¹

<http://documents.worldbank.org/curated/en/327881470142199866/pdf/AUS16696-WP-OUO-9-Ukraine-CEA-has-been-approved-P151337.pdf>.

¹⁷ IFC Performance Standard 1, January 2012, para. 7.

¹⁸ Danosha Non-Technical Summary, May 2014, available at: <http://www.danosha.com.ua/images/reports/05-2014-en.pdf>.

¹⁹ IFC Access to Information Policy, January 2012, para. 31.

²⁰ IFC Performance Standard 3, January 2012, para. 4. Good international industry practice include the World Bank Group Environmental, Health and Safety Guidelines.

²¹ IFC Performance Standard 4, January 2012, para. 5.

Regarding agribusiness operations, the World Bank EHS Guidelines state that manure contains nitrogen, phosphorus, and other excreted substances which may result in air emissions of ammonia and other gases and may pose a potential risk of contamination to surface or groundwater resources through leaching and runoff. It adds that manure contains disease-causing agents such as bacteria, pathogens, viruses, parasites, and prions which may potentially affect soil, water, and plant resources (for human, livestock, or wildlife consumption). The use of manure as a fertilizer on agricultural land requires careful assessment of potential impacts due to the presence of hazardous chemical and biological constituents.²²

The project ESRS states that the “*design of the lagoons, with fixed double bottom liners with leak control and a single floating top liner, as well as the design of the field pumping systems prevent smell during the storage of the manure, and also prevent raw manure from spilling into water courses.*” The ESRS, while acknowledging the potential for odor nuisance and inherent risks of manure pumping methods, describes measures for odor mitigation and spill prevention. Such methods include, inter alia, use of modern hose equipment, manure application by injection, pumping systems equipped with automatic shutoff and on-duty guards at river/creek passing.

As for crop production, the ESRS notes that “*modern state-of-the-art production principles*” are used for manure application in spring and autumn when crops are ready to absorb the nutrients and runoff can be avoided. The ESRS further explains that to ensure optimal nutrient balances for land application, approximately one hectare is required per sow.²³ Harvested crops include barley and wheat, among others, as well as non-feed-related crops “*to ensure the appropriate crop rotation to improve the soil quality.*” According to the ESRS, fertilizer application is controlled by computerized management tools and non-application zones enforced near drains, water channels and rivers to prevent water contamination.

In relation to monitoring and testing, the ESRS notes that individual water wells are tested and if necessary, treated prior to use in animal production. It further notes that emission, smell and local waterway testing is conducted on a routine basis and reported to relevant authorities.

Client commitments under the ESAP include: (i) fertilizer usage in accordance with EU principles and local regulations; (ii) liquid effluent control; and, (iii) manure application control, ensuring harmonization between animal hold, manure production and farmed crop land. IFC notes its requirements for the client to conduct periodic air, water and soil testing. IFC informed CAO that, the client has engaged a laboratory with a mobile unit that regularly conducts testing at the client’s farms for this purpose.

In response to air, water, and soil pollution concerns, IFC notes manure application occurs twice yearly, subject to seasonal, climatic and holiday restrictions. According to IFC, testing of environmental parameters demonstrate compliance with national law.

Water. IFC acknowledges the client exceeded permissible ammonia levels in surface waters at Luka farm in select months in 2015 and 2016. In response to these deviations, IFC notes the client has taken precautionary measures to prevent potential leakages at manure lagoon sites. In addition to deviations in surface water, CAO notes there has been fluctuations in results of potable water testing, specifically in relation to sanitary chemical and microbiological indexes. IFC maintains that, based on monitoring and review of testing data, exceedances in permissible levels have occurred and corrective measures have been implemented.

²² World Bank Group Environmental, Health, and Safety Guidelines for Mammalian Livestock Production, April 30, 2017, page 3.

²³ A sow is an adult female pig. As explained by IFC, approximately one hectare is required per sow in production with all its offspring, from piglets to hogs, at any given time.

Soil. In response to complainants' concern regarding soil degradation, IFC is of the view that the client's operation contributes to improving soil quality of land plots through manure fertilization. IFC has provided CAO with data and documentation showing increase in crop production as an indication of improvement of soil quality. This includes: a report by local authorities on soil improvement, crop yield progression from 2013 to 2017 for all of the client's farms, a sample of commercial fertilizer usage for the period 2015 to 2017 showing that additional fertilizer was needed besides the manure, and the clients soil quality investigation reports. IFC also provided CAO with sample slurry (manure) analysis. IFC considers that soil testing is being conducted according to required permit parameters. CAO acknowledges that information on soil condition indexes as well as veterinary, sanitary and epidemiological testing is available. CAO also acknowledges that the data indicates yield progression and soil quality improvement.

Air. IFC notes that the company has implemented odor mitigation approaches at different stages of swine production, manure storage and handling and land application, including the use of new technologies to minimize odor nuisance and air pollution. In addition, IFC reports that the company monitors ambient air quality on a quarterly basis, results of which do not exceed applicable standards. CAO notes that aside from the ongoing judicial proceedings, air testing documentation reviewed during this appraisal does not indicate instances of non-compliance.

While acknowledging information provided by IFC in relation to the client's approach to pollution control and monitoring, CAO has questions as whether this meets good international industry practice as required by PS3 and PS4. Technical review of the client's ESMS, monitoring protocols, and monitoring results is required to confirm this in relation to water, soil and air pollution risks.

Water Extraction

The complainants allege that the client's water extraction has contributed to wells drying out and groundwater depleting, which impacts the community water resources and well-being.

As a general matter, IFC requires its clients to adopt resource efficiency and water reduction measures so as not to have significant adverse effects on water access for local communities.²⁴ Resource efficiency techniques, including those related to water use, should meet good international industry practice.²⁵ PS1 also requires that the cumulative impacts of a project should be identified.²⁶

The project ESRS states that most of the client's farms have their own water wells established based on hydro-geological acceptance and water permits. IFC shared with CAO data showing that the client is electronically monitoring its water consumption at several points. IFC maintains all farms have necessary water use permits (potable and non-potable). However, IFC also notes that groundwater depletion remains a public concern region wide. The client commissioned a hydrogeological assessment in June 2017, which assesses the potential impact of nearby quarries on water intake of the client's operations. The client also indicates that Halych authorities have initiated the development of water pipelines to villages of the district. The client is a working group member, providing knowledge, experience and financial support for the project.

While IFC and the client have provided documentation and narrative to CAO in relation to the client's water use, it remains unclear to CAO whether IFC has assurance that potential impacts of the client's water use have been assessed and mitigated in accordance with IFC requirements.

Halych National Nature Park

²⁴ IFC Performance Standard 3, January 2012, para. 9; and IFC Guidance Note 3, January 2012, para. 25 & 26.

²⁵ IFC Performance Standard 3, January 2012, para. 4

²⁶ IFC Performance Standard 1, January 2012, para. 8.

The complainants raise concerns about potential environmental impact on the Halych National Nature Park and lack of consultation with the protected area representatives. In general, the complainants allege violation of PS6, particularly in relation to the assessment and mitigation of impacts on biodiversity and ecosystem services in areas of high environmental danger.

Relevant to PS6 (Biodiversity Conservation and Sustainable Management of Living Natural Resources), the complainants allege that the project is: (i) within immediate proximity of Halych National Nature Park, with potentially significant impact to biodiversity and ecosystem services and (ii) contributing to increased levels of anthropogenic impact.

PS6 scope of application includes projects “(i) located in modified, natural, and critical habitats; (ii) that potentially impact on or are dependent on ecosystem services over which the client has direct management control or significant influence; or (iii) that include the production of living natural resources (e.g., agriculture, animal husbandry, fisheries, forestry).”²⁷ IFC guidance on PS6 adds that the risks and impacts identification process will vary depending on the nature and scale of the project. At a minimum, the client should screen and assess the risks to and potential impacts on biodiversity and ecosystem services in the project area of influence, taking into account, among others, “the location and scale of project activities” and “the project’s proximity to areas of known biodiversity value or areas known to provide ecosystem services.”²⁸

At time of disclosure, IFC deemed PS6 non-applicable. IFC takes the view that the project does not impact nor operate inside park boundaries. IFC notes that Halych National Nature Park does not extend over a contiguous area and various patches of the Park are of different biodiversity value. IFC provided CAO satellite imagery showing the location of the park in relation to Delievo and Lany farms. IFC points out that the farms are in proximity of areas classified as “economic activity zone” or “regulated recreation zone” and not in proximity of any “preserved zone”. IFC also notes that the client has obtained necessary approvals from relevant state authorities, including for those farms located nearest to the national park.

Although the ESIA did not adequately identify nature reserves in the vicinity of the project, the CAO compliance team observed the forest belt during its visit. The Halych National Nature Park is composed of patches of forests, two of which are in close proximity to the Delievo and Lany farm facilities; respectively at 10m and 250m distance from the facilities.

According to information made available to CAO, a court decision dated May 23, 2013, suggests tree felling and disturbance to forest duff occurred within national park bounds in 2012, for which the client was subsequently fined. CAO acknowledges this was an accidental and seemingly unique occurrence.

CAO’s review of IFC project documentation, including the imagery provided and the zoning classification in proximity of the farms, indicates that, based on the information available at the time of the investment, IFC identified potential concerns regarding the location of the national park and conducted reasonable analysis to exclude the application of PS6. On this basis, CAO has determined to close this issue at appraisal.

Road-related Impacts

The complainants allege that the client’s large trucks are causing road wear, dust pollution and traffic vibrations. They add that the traffic-related dust emission is impacting public health and well-being and that the vibrations are causing structural damage to nearby houses. The complainants contend that the refurbishment of a field road and road-side drain near Luka farm led to loss of access to their plots and encroachment on privately-owned land plots.

²⁷ IFC Performance Standard 6, January 2012, para. 5

²⁸ IFC Guidance Note 6, January 2012, para. 5.

PS4 requires clients to evaluate the risks and impacts to the health and safety of the affected communities during the project life-cycle and establish preventive and control measures consistent with GIIP, such as in the World Bank Group (EHS) Guidelines or other internationally recognized sources. Also, PS4 requires the client to identify risks and impacts and propose mitigation measures that are commensurate with their nature and magnitude. These measures will favor the avoidance of risks and impacts over minimization.²⁹

PS1 requires clients to anticipate and avoid risks and impacts. Where avoidance is not possible, it requires the client to minimize it, and, where residual impacts remain, compensate or offset wherever technically and financially feasible.³⁰

In relation to community concerns for health and safety, the ESRS recognizes “*movement of large scale machines*” is occurring near farms and on minor roads “*in areas of low population density, and inhabited by farmer families used to the nature of large scale agricultural machinery.*” The ESRS notes that significant economic support is given in the form of road improvements and public areas clearing in the wintertime.

At meetings community members voiced their dissatisfaction with the quality of road work funded by the client and quantity of associated funds. However, community members acknowledged there are two additional companies using the same roads for their operations. While acknowledging controlled vehicle movement to and from farms, the client informed CAO of its support for the maintenance and repair of roads through the community fund. IFC maintains that overall responsibility for road conditions falls upon relevant local administration and remains an ongoing challenge throughout Ukraine. IFC places emphasis on the client’s contributions to road maintenance and repairs through its social fund. The fund, as explained to CAO, allocates thirty percent for this purpose and is often earmarked for specific road repairs.

The project ESRS acknowledges the issue of road wear impact. CAO notes that the client’s control of vehicle movement to and from farms is designed to minimize this impact. CAO also notes that the client’s maintenance and repairs program through its social fund is designed to offset residual impacts stemming from road traffic, although the adequacy of the offset program is not clear.

As regards land encroachment and access claims specific to Sivka-Voynylivska village, the client explains that, in agreement with an established road commission in 2009, it refurbished a field road to access Luka farm facilities and fields. According to the client, subsequent to reconstruction, a roadside drain was dug and a number of access points were constructed to provide ease of access to land plots. The client contends that amid community complaints in 2014, the road commission reengaged to investigate potential road deviation from the original agreement. According to the client, the allegations were deemed to be unsubstantiated with no grounds for compensation. The client has, however, expressed intention to contact the Sivka-Voynylivska village council and roadside land owners to ensure their access to land plots.

CAO notes that the alleged encroachment over privately-owned plots has been investigated by the road commission as mandated by local authorities. CAO notes the findings of the road commission determined that no encroachment had occurred. CAO also notes that the alleged encroachment occurred prior to IFC’s investment.

On the basis of the above considerations, CAO has determined to close the issues related to land encroachment at appraisal. Issues related to management and mitigation of road impacts (dust, cracks, and road wear) will be analyzed as part of CAO’s review of the client’s ESMS.

²⁹ IFC Performance Standard 4, January 2012, para. 5.

³⁰ IFC Performance Standard 1, January 2012, para. 14.

Land-use and Associated Compensation

The complainants contend that the client: i) cultivated privately-owned land plots without prior agreement or adequate compensation; ii) improperly used land resulting in access restriction to plots; and iii) failed to restore land which was altered, degraded or polluted. They argue that the client's operation, as it relates to land-use, is non-compliant with national legal requirements of Ukraine.

As relates to leased land, IFC did not identify E&S risks or impacts during its due diligence process. Generally, IFC maintains that a significant portion of land-use related disputes have been formally registered in the complaint log and adequately handled through the client's grievance mechanism. More specifically, of the 131 land plots under dispute (76 complainants), 96 were either invalidated or compensated for and 20 land plots remain unclaimed by relatives of deceased plot owner(s). IFC indicates that the client assists family members who seek to establish inheritance rights. Overall, fifteen plots remain under dispute over issues of compensation. These relate to land plots located in Sivka-Voynylivsk that were cultivated by the client between 2005-2012. According to IFC, all land owners compensated for past use were paid full inflation-adjusted compensation.

It should be noted that, during the site visit, CAO encountered one affected community member in Delievo village, alleging that a water pipe had been laid without the owner's prior consent and without compensation. The land owner had not attempted to resolve the dispute through the client's established grievance mechanism. Whilst CAO requested affected community members with concerns about the use of their plots to come forward, no others have done so to date.

CAO notes that the client is open to and has sought to resolve any land-related pending issues. Where consensus has not been achieved with land plot owners, the client physically delineates the border with posts to prevent cultivation. CAO therefore has determined to close this issue at appraisal without further investigation. Should any affected community members come forward, further investigation may be justified.

Stakeholder Engagement and Grievance Mechanism

The complainants allege that the client does not have a grievance mechanism. They claim that communication between affected communities and the client throughout project planning, development, and operation was limited.

PS1 requires the client to provide Affected Communities "*access to relevant information on [...] the grievance mechanism.*"³¹ PS1 makes provision for the establishment of a grievance mechanism by the client. The grievance mechanism should be easily accessible, understandable and its availability communicated to affected communities.³²

The ESRS states that general disclosure will take place on the client's website and will make the ESRS/ESAP review locally available in Ukrainian at the client's headquarters. The ESAP required the client to facilitate the online registration of complaints, including expected response time. In February 2014, the client developed internal corporate-level grievance procedures.

In February 2014, the client developed internal corporate-level grievance procedures as agreed in the ESAP. CAO confirms the client provides an email address on its webpage to receive concerns, with specified response period of thirty days. The client informed CAO that it has appointed thirteen community representatives and that it operates three additional grievance access points: (i) two telephone hotlines, one for each district (Kalush and Halych); (ii) complaint

³¹ IFC Performance Standard 1, January 2012, para. 29.

³² IFC Performance Standard 1, January 2012, para. 35.

boxes (at village councils); and (iii) community surveys. The client has maintained a complaint log since 2013, most of which contain complaints pertaining to land, as noted by IFC.

On the basis of the above considerations, CAO has determined to close aspects related to stakeholder engagement and grievance mechanism. These aspects being analyzed separately from the disclosure of environmental information relevant to affected community members and consultation over such information.

IV. CAO Decision

The purpose of a CAO compliance appraisal is to determine whether an investigation of IFC's E&S performance is required in response to a complaint. In deciding whether to initiate an investigation, CAO weighs factors including the magnitude of the E&S concerns raised in a complaint, results of a preliminary review of IFC's E&S performance in relation to these issues, and a more general assessment of whether a compliance investigation is the appropriate response in the circumstances.

The complaint alleges violation of IFC Performance Standards 1, 3, 4 and 6, with respect to: (1) environmental and social assessment and management system; (2) air, water and soil pollution; (3) water extraction; (4) Halych National Nature Park; (5) road wear, cracks, dust emission, access and land encroachment; (6) land use and associated compensation; and (7) stakeholder engagement and grievance mechanism.

CAO has identified concerns as to IFC's review and supervision of the project. While having decided to close specific issues in relation to impacts to the Halych National Nature Park, road encroachment, land use, and stakeholder engagement and grievance mechanism, CAO will conduct an investigation of IFC's E&S performance in relation to the remaining issues. Thus, the investigation will focus on the adequacy of:

- IFC's review and supervision of the client's ESMS, including measures to ensure that procedures are in place to test for, and mitigate against, environmental pollutants;
- IFC's review of the (i) ESIA documentation (including water extraction, carrying capacity and manure management system) and (ii) associated consultation and disclosure, where relevant;

CAO notes that the decision to initiate a compliance investigation does not imply a finding in relation to the client's E&S performance adverse or otherwise.

Terms of Reference for this compliance investigation will be issued in accordance with CAO's Operational Guidelines.