



December 13, 2021
Office of the Compliance Advisor Ombudsman (CAO)

COMPLIANCE APPRAISAL: SUMMARY OF RESULTS

Adjaristsqali Hydropower Cascade Project, Georgia (IFC Projects #30428, 33435, 37781 & 601449; MIGA Project #12315).

Complaint AGL-01/Makhalakidzeebi

Background

The Shuakhevi hydropower project (Shuakhevi HPP/the project) is a 184 megawatt (MW) hydropower scheme comprised of two dams with reservoirs in the Adjaristsqali and Skhalta Rivers, a weir on the Chirukhistskali River, and a total of 33.8 kilometers (km) of underground tunnels. The project is located in the Adjaristsqali region of the Autonomous Republic of Adjara in southwest Georgia. It is implemented by Adjaristsqali Georgia LLC (AGL), a special purpose vehicle (SPV) owned by Clean Energy Invest of Norway, Tata Power of India, and (previously) the International Finance Corporation (IFC).

The total project cost was estimated to be US\$427 million. In 2014, IFC, the European Bank for Reconstruction and Development ([EBRD](#)), and the Asian Development Bank ([ADB](#)) (the lenders) made loans to support the construction of the project. IFC's investment, as approved, consisted of a loan of up to US\$71 million and an equity investment of up to US\$34 million (IFC projects #33435 and #37781). The investment aimed to:

- a) increase Georgia's renewable energy output;
- b) reduce GHG emissions;
- c) influence Georgia's ability to attract foreign investments in the hydropower sector; and
- d) contribute to private sector investments in Georgia, including South-South investments.

Project construction commenced in 2014 and was completed in 2020. In April 2020, IFC sold its shares in AGL and exited the equity investment. IFC's loan remains active. In addition, the Multilateral Investment Guarantee Agency (MIGA) provided a US\$63 million guarantee to Tata Power International Pte. Ltd. to cover its equity investment in the Project (MIGA project #12315). MIGA's guarantee also remains active.

In February 2018, CAO received a complaint from 17 community members living in the Rabati District of the Makhalakidzeebi village, Shuakhevi Municipality, Adjara, Georgia. The complaint alleges several actual and anticipated negative impacts to the residents of Makhalakidzeebi and the local environment as a result of the development of the Shuakhevi HPP. The key concerns raised by the complainants include:

- Increased risk of landslides and rockfalls allegedly caused by the construction and explosions carried out during tunneling works, posing threat to the safety of the community.
- Reduction in groundwater flows due to construction (tunneling), resulting in loss of access to water for drinking, household use, and irrigation in the Makhalakidzebi community.
- Negative impacts on the biodiversity of the Adjaristsqali river, resulting in the disappearance of several fish species, including an endangered species of trout, and trees.

The same complaint was also filed with EBRD's and ADB's accountability mechanisms (the Project Complaint Mechanism (PCM) and the Office of the Special Project Facilitator (OSPF), respectively). However, both mechanisms closed their cases after attempts at dispute resolution were unsuccessful. Two civil society organizations also submitted an additional complaint regarding the Shuakhevi project to EBRD's PCM in July 2018.¹ The civil society complaint raises similar issues regarding environmental and social (E&S) assessment and management; landslides, groundwater availability; and biodiversity impacts.² At the time of writing this appraisal report, a compliance review of EBRD's investment in this project was being conducted by EBRD's PCM.

This complaint was referred to the CAO compliance function for appraisal following an unsuccessful attempt at a CAO facilitated dispute resolution process that took place between June 2018 and August 2020.

Approach

Following transitional arrangements agreed as part of the approval of the new CAO policy in June 2021, this compliance appraisal is being conducted following CAO's 2013 Operational Guidelines. Under the Operational Guidelines, the purpose of a CAO compliance appraisal is to ensure that compliance investigations are initiated only in relation to projects that raise substantial concerns regarding E&S outcomes and/or issues of systemic importance to IFC/MIGA. In deciding whether to initiate a compliance investigation, CAO weighs various factors including the magnitude of the E&S concerns raised in a complaint, the results of a preliminary review of IFC's E&S performance in relation to these issues, the existence of questions regarding the adequacy of IFC's requirements, and a more general assessment of whether a compliance investigation is the appropriate response in the circumstances.

In reaching a decision on whether a compliance investigation is merited, this appraisal has considered IFC's approach to E&S review and supervision of the project as relevant to the specific issues raised in the complaint. The lenders hired a third-party consultancy, an international environmental and social consultant (IESC) to provide support during due diligence and monitoring of the project. During the pre-investment stage, IFC and the other lenders conducted a site visit and were supported by the IESC, to review the project's E&S documentation. The lenders agreed with the client on an E&S Action Plan (ESAP) to address gaps found during the project appraisal. During supervision, the IESC conducted site visits and monitored the project on the lenders' behalf.

Analysis

1 EBRD, Project Complaint Mechanism Shuakhevi HPP (Request #2). Available at <https://bit.ly/32Oclff>

2 EBRD, Project Complaint Mechanism Eligibility Assessment Report. Available at <https://bit.ly/3rw6F9g>

CAO conducted a preliminary analysis of the concerns raised by the complainants in relation to landslides and rockfalls, groundwater flows, and biodiversity impacts, which is summarized below:

Landslides and rockfalls: The complainants raised concerns that the explosions carried out during the construction of the project would increase the risk of landslides and rockfalls in Makhalakidzebi village, posing threats to their safety. The Environmental and Social Impact Assessment (ESIA) for the project identifies the Adjara region as prone to landslides and erosion. In response, AGL conducted geological and topographic studies to ensure the project design would minimize the risk of landslides. AGL put in place a range of measures, including the use of low-energy explosives and hard rock excavation to reduce landslide risk. In response to visual observations and community requests, AGL installed ground monitoring monuments, landslide monitoring systems, and conducted periodic site monitoring, in addition to inspecting houses located along the tunnel alignment prior to and after tunnel construction. Based on a preliminary review of project documentation and interviews with the complainants, it appears that no landslide damage was recorded in Makhalakidzebi village during the construction of the project.

Considering the risk management measures outlined above, information received from the complainants, and the fact that the construction phase has ended, CAO concludes that this issue does not require a compliance investigation. Nonetheless, CAO encourages IFC to ensure that regular geological reviews are properly conducted for the first 10 years of operation — as suggested by the ESIA — in order to ensure that any ongoing landslide risk associated with the project is appropriately monitored and mitigated.

Groundwater flows: The complainants allege that the construction of the project has caused scarcity of spring water sources in their village, with adverse impacts on access to water for drinking and irrigation. The complainants rely significantly on spring water for household and agricultural consumption. Impacts on water sources were the complainants' primary concern at the time of writing this compliance appraisal. The ESIA noted that during the construction there could be substantial impacts on areas where the tunnel is closest to the surface including impacts on water resources for drinking, irrigation, and household use, and that temporary or permanent drainage of water wells could occur. The ESIA recommends mitigation measures in relation to these potential impacts. AGL conducted spring water monitoring during construction as a condition of its environmental permit. Given continued community grievances on this issue, the IESC recommended that the client hire an independent consultant to assess whether the project has an impact on water sources. While the IESC documentation does not mention the results of the recommended study, the IESC later noted that the client was conducting its own spring water monitoring, which was described as rudimentary. A review of IFC supervision documentation raises questions regarding the adequacy of baseline data as required to assess project impacts on access to groundwater.

Based on available documentation, CAO has questions as to the adequacy of IFC's review and supervision of the potential impacts of the project on spring water, and the associated mitigation measures proposed. As a result, CAO concludes that the water scarcity raised by the complainants warrant a compliance investigation.

Biodiversity impacts: The complainants allege that the construction of the project has negatively impacted freshwater fish populations, including an endangered trout species. They also provided information to the CAO compliance team about the destruction of trees as a result of the project. The project is located in a river that IFC identified as a "critical habitat." When undertaking a project in critical habitat, IFC Performance Standard (PS) 6 on Biodiversity Conservation and

Sustainable Management of Living Natural Resources establishes stringent requirements for avoiding, mitigating, and offsetting project impacts on sensitive ecosystems. The ESIA notes that the project could significantly impact biodiversity and ecosystem services in the area. However, these impacts would be significantly reduced through the implementation of the proposed mitigation measures. Since 2015 the IESC has raised concerns regarding the adequacy of the client's reporting as needed to identify project impacts on biodiversity in the project area. In this context, the IESC recommended that the client hire an international consultant to review and analyze the biodiversity data from beginning of construction until 2018. The consultant found a decline in the number of species in the Chirukhistsqali River and changes in fish abundance during the construction period. While the IESC found it premature to associate the declines/abundances with the project, the IESC stated that further monitoring was needed. In 2019, the client presented a Corrective Action Plan (CAP) to address this issue. As of IFC's last supervision virtual visit (September 2020), the IESC reported that compliance with the CAP still needed to be addressed. In this context, CAO has questions as to whether IFC obtained necessary information to assess the status of project's compliance with the Performance Standards and whether IFC's supervision was adequate to assess and address potential project impacts on riverine biodiversity in the project area of influence.

Appraisal Result

Based on a preliminary review of available information, CAO concludes that a compliance investigation is warranted in this case. CAO finds that the issues raised by the complainants regarding project impacts on groundwater flows and biodiversity are potentially significant in nature given: (a) the complainants' reliance on groundwater for household and agricultural use; and (b) the location of the project in critical habitat. CAO's preliminary analysis of the complaint also raises questions regarding the adequacy of IFC's E&S review and supervision of the project as relevant to project impacts on groundwater and biodiversity.

Terms of Reference for the compliance investigation are attached in Annex 1.

About CAO

The Office of the Compliance Advisor Ombudsman (CAO) is the independent recourse and accountability mechanism for the International Finance Corporation (IFC) and Multilateral Investment Guarantee Agency (MIGA), members of the World Bank Group. CAO addresses complaints from people who may be affected by the environmental and social impacts of projects supported by IFC/MIGA. CAO reports directly to the Boards of IFC and MIGA (the Board) and is fully independent of IFC/MIGA management.

CAO was established in 1999. As of July 2021, CAO carries out its work in accordance with [the IFC/MIGA Accountability Mechanism Policy](#) (the CAO Policy).

Through the exercise of its dispute resolution, compliance, and advisory functions, CAO's mandate is to:

- facilitate the resolution of complaints from people who may be affected by IFC/MIGA projects or sub-projects in a manner that is fair, objective, and constructive;
- enhance the environmental and social outcomes of projects in which those institutions play a role; and
- foster public accountability and learning to enhance the environmental and social performance of IFC and MIGA and reduce the risk of harm to people and the environment.

CAO's Compliance Function

The purpose of the CAO compliance function is to carry out reviews of IFC/MIGA's compliance with E&S Policies, assess related harm, and recommend remedial actions where appropriate.³ The CAO compliance function follows a three-step approach:

(1) A compliance appraisal, which determines whether further investigation is warranted. If warranted, the appraisal is followed by an investigation.

(2) A compliance investigation determines whether IFC/MIGA has complied with its E&S Policies and whether there is harm related to any IFC/MIGA non-compliance.

(3) Compliance monitoring to monitor implementation of corrective actions approved as part of the Management Action Plan approved by the Board.⁴

Following transitional arrangements agreed as part of the implementation of the 2021 CAO Policy, this compliance appraisal report was prepared following CAO's 2013 [Operational Guidelines](#).⁵

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

³ IFC/MIGA Independent Accountability Mechanism (CAO) Policy, para. 76.

⁴ Ibid, para. 79.

⁵ CAO Transitional Arrangements were published in July 2021 and are available at <https://bit.ly/3rusRRq>

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Acronyms

Acronym	Definition
ADB	Asian Development Bank
AGL	Adjaristsqali Georgia LLC
BAP	Biodiversity Action Plan
CAO	Office of the Compliance Advisor Ombudsman (IFC and MIGA)
CEMP	Construction Environmental Management Plan
EBRD	European Bank for Reconstruction and Development
E&S	Environmental and Social
EHS	Environmental, Health and Safety
EMS	Environmental Management System
ESIA	Environmental and Social Impact Assessment
ESAP	Environmental and Social Action Plan
ESDD	Environmental and Social Due Diligence
ESMP	Environmental and Social Management Plan
ESMS	Environmental and Social Management System
ESRS	Environmental and Social Review Summary
ESRP	Environmental and Social Review Procedures
HPP	Hydro Power Plant
H&S	Health and Safety
IESC	Independent Environmental and Social Consultant
IFC	International Finance Corporation
IFI	International Finance Institution
MIGA	Multilateral Investment Guarantee Agency
MOU	Memorandum of Understanding
NGO	Non-Governmental Organization
O&M	Operational and Maintenance
PCM	Project Complaint Mechanism (EBRD)
PS	Performance Standards (IFC)
SEP	Stakeholder Engagement Plan
SPV	Special Purpose Vehicle
OSPF	Office of the Special Project Facilitator (ADB)

I. Overview of the Compliance Appraisal Process

As noted above, following transitional arrangements agreed upon as part of the implementation of the 2021 CAO Policy, this compliance appraisal report was prepared following CAO's 2013 Operational Guidelines.

When CAO receives a complaint about an IFC or MIGA project, the complaint goes through an assessment process. 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.

In order to decide whether a compliance investigation is warranted, CAO first conducts a compliance appraisal. The purpose of the 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.

CAO applies several basic criteria to guide the compliance appraisal process. 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.

II. Background

Investment

The Adjaristsqali Georgia LLC (AGL or the company) is a special purpose vehicle (SPV) owned by Clean Energy Invest of Norway and Tata Power of India.⁶ AGL is implementing the Shuakhevi project, a 184 MW hydropower scheme comprised of two dams (39 meters (m) and 22m in height, respectively) with reservoirs in the Adjaristsqali and Skhalta Rivers—a 5m weir on the Chirukhistiskali River and a total of 33.8 km of underground tunnels.⁷ The Shuakhevi project also involved the construction of 5.9 km of new roads and four new bridges and construction camps. The scheme is located in the Adjaristsqali region of the Autonomous Republic of Adjara in southwest Georgia.

The total project cost was estimated to be US\$427 million. Starting in 2011, IFC assisted with project development through its InfraVentures project development fund (IFC project #30428).⁸ The objective of the IFC InfraVentures engagement was to assist with preparatory activities to support the project in securing finance for construction. Starting in 2014, IFC, EBRD and ADB (the lenders) provided loans to support project construction.⁹ IFC's investment, as approved, consisted of an A loan of up to US\$71 million and equity of up to US\$34 million (IFC project #33435 and #37781).¹⁰ IFC acted as the lead arranger of the financing.¹¹ IFC also had an Advisory Services project to advise on AGL's retrenchment strategy for demobilization of the construction workforce and associated implementation plans, including sustainable livelihood opportunities for the communities and workforce (IFC project #601449).¹² In addition, MIGA is providing a \$63 million guarantee to Tata Power International Pte. Ltd. to cover its equity investment in the Project (MIGA project #12315).¹³

In December 2016, IFC completed its advisory services engagement with AGL. In April 2020, IFC sold its share in AGL, thus exiting the equity investment. Therefore, both IFC's equity and advisory projects (#37781 and #601449) are closed, while IFC's A loan and MIGA's guarantee remain active at the time of writing this report (#33435 and #12315).

Construction of the project began in June 2014 and, the project started operation in March 2020.

The Complaint

The Complainants' Perspective

In February 2018, CAO received a complaint from residents of Rabati District of Makhalakidzebi village, Shuakhevi Municipality, Adjara, Georgia.¹⁴ The complainants represent 22 households,

⁶ IFC Summary of Investment Information (SII), Adjaristsqali Georgia LLC, Project #33435 <https://bit.ly/3dcn9eL>

⁷ *Ibid.*

⁸ IFC InfraVenture is "a global infrastructure project development fund that has been created as part of World Bank Group's efforts to increase the pipeline of bankable projects in developing countries. Its unique offering, combining early-stage risk capital and experienced project development support, is designed to address the key constraints to private investment in infrastructure projects in frontier markets", <https://bit.ly/3pogbc1>

⁹ Senior loans from IFC, EBRD and ADB ("the Lenders") account for \$80 million, \$90 million and \$90 million respectively, another B loan/parallel loans of \$40 million and Sponsor equity of \$127 million.

¹⁰ IFC processed debt and equity investment jointly under project #33435, including project information disclosure.

¹¹ The investment also consists of a B/Parallel Loan of up to US\$220 million, IFC (SII), <https://bit.ly/3xRLHmS>

¹² IFC, Summary of Advisory Service and Project Information, <https://bit.ly/3oq0kuB>. CAO does not consider this Advisory Service project further as it is not relevant to the issues raised in the complaint.

¹³ Multilateral Investment Guarantee Agency, Adjaristsqali Hydro Project, Project description, <https://bit.ly/3lhR3wg>

¹⁴ CAO Assessment Report, AGL-01/Makhalakidzebi, July 2018, <https://bit.ly/3rqpCdQ>

located less than 500 meters from one of the project's tunnels. The complaint alleges several current and potential negative impacts to the residents of Makhalakidzeebi and the local environment as a result of the project's construction and operation. The complainants allege that they have raised their complaints with the company and requested for geological studies to be conducted without receiving any feedback or response.¹⁵ The complainants and the company went through a CAO-supported dispute resolution process. As an agreement was not reached, the complaint was transferred to the compliance function, according to CAO's Operational Guidelines.¹⁶ The complaint raises the following concerns:

- i. **Landslides and Rockfalls**: The region where the project is located is prone to landslides and rockfalls. The complaint raises concerns that tunneling works increased the frequency of landslides and rockfalls, posing a threat to their safety. The complainants state that the project started construction without detailed geological studies to assess the potential risks. They allege that the project's impacts are so serious that peoples' lives and the survival of the Makhalakidzeebi village are at risk. In CAO's assessment report, the complainants raise concerns regarding vibration from AGL's blasting and drilling activities damaging private houses and shelters in the village. However, as explained to CAO staff during the compliance appraisal, only minor damage was experienced and no landslide-related damage occurred in Makhalakidzeebi village, during project construction.
- ii. **Groundwater Flow**: The complainants allege that the project impacted spring water sources, leaving the Makhalakidzeebi community with insufficient water for drinking and irrigation. They state that 7 different spring water sources have disappeared in the area because of the project, and that approximately 100 people from 22 households in the Rabati District do not have enough water to support their basic needs. The complainants claim that the loss of access to water for irrigation caused a reduction in the volume and quality of their harvest, with serious consequences for the subsistence of villagers. They further allege that the government of Adjara and AGL provide poor quality water to the community. They state that, in 2014, the Government of Adjara, AGL, and the Makhalakidzeebi village entered into an agreement to regulate their respective obligations with regard to the implementation of the project. The company committed to survey the water supply in the village and remediate the negative water supply impacts attributable to the project, including resettling affected households in case water supply could not be provided.¹⁷ The complainants indicated to CAO that AGL offered compensation for the loss of potable water, but that they refused as they deemed the amount to be disproportionately low given the negative impacts.
- iii. **Impacts on Biodiversity**: The complainants allege that project construction has had negative impacts on biodiversity. They note disappearance of fish in the Adjaristsqali river, including an endangered species of trout. They also allege that discharges from the construction of the project caused trees to die.

¹⁵ CAO Assessment Report, AGL-01/Makhalakidzeebi, July 2018, <https://bit.ly/3oheePv>

¹⁶ CAO Operational Guidelines, Section 2.4, Step 4 (a), 2013. <https://bit.ly/3lr6C59>

¹⁷ Agreement Between Government of Adjara A.R., Adjaristsqali Georgia LLC and residents of Makhalakidzeebi Village, May 1, 2014, Article 2.

The Company's Perspective

AGL states that any damages to houses were not caused by the project. They state that a joint committee of government officials, community representatives, and independent geological experts conducted inspections on the houses located along the tunnel alignment prior to, and after, the construction of the tunnels in 2014 and 2016. According to the company, the inspection concluded that damage to the houses was due to natural causes and not directly related to AGL's construction. However, as part of its corporate social responsibility program, the company partnered with the local government and offered to contribute to a resettlement program initiated by the mayor's office. AGL indicated that it provided GEL 5000 (USD approx. \$1500) to the local government to support a resettlement program for households impacted by landslides in the area of the project.

Regarding water scarcity, AGL indicated that from 2014 to date, it has regularly monitored the spring water flow in the Makhalakidzebi village and has been sharing monitoring reports with Georgia's Ministry of Environment on a monthly basis. According to AGL, the experts who carried out the water monitoring could not find any link between AGL's activities and the decrease in groundwater levels in the village. However, AGL explained that it acknowledges the water scarcity problem affecting the village and, in response, has initiated and implemented two water supply rehabilitation projects in partnership with the mayor's office.

In relation to the complainants' claim that the project has had negative impacts on the biodiversity of the Adjaristsqali river, AGL argued that the claim is irrelevant since the community is located near the Chirukhistsqali river. Further, AGL stated that it regularly monitors impacts on the biodiversity of all three local rivers, including the Adjaristsqali, and that the data do not show any changes or concerns. At the time of CAO's assessment, the company noted that the project had not reached commercial operations yet, hence the question of negative impacts on the river biodiversity due to water diversion was irrelevant and baseless.

Complaints to Other Development Banks

In 2018, the complainants also submitted complaints to the EBRD's Project Complaint Mechanism (PCM)¹⁸ and the ADB's Office of the Special Project Facilitator (OSPF).¹⁹ These complaints were closed following dispute resolution processes conducted by PCM and OSPF.

An additional complaint regarding the Shuakhevi project was submitted to PCM's compliance review function in July 2018 by two civil society organizations, Green Alternative and CEE Bankwatch Network.²⁰ This complaint raised broader issues regarding the environmental and social impacts of the project including some similar concerns to those raised in the CAO complaint regarding landslides, groundwater availability, and biodiversity impacts.²¹ As at the time of writing, PCM was conducting a compliance review of that complaint.

III. IFC's Pre-Investment Review and Supervision of the Project

¹⁸ In July 2020, the PCM was replaced by the Independent Project Accountability Mechanism (IPAM)

¹⁹ IPAM, Shuakhevi HPP, Case Registry, <https://bit.ly/3xNiXLO> and ADB, Accountability Mechanism, Complaints Registry by Project, <https://bit.ly/3lbbk6V>

²⁰ EBRD, Project Complaint Mechanism Shuakhevi HPP (Request #2). Available at <https://bit.ly/3Ekjvwv>

²¹ EBRD, Project Complaint Mechanism Assessment Report. Available at <https://bit.ly/3oggKW4>

This section outlines IFC and MIGA's E&S policies and procedures as they apply to the project. It also provides a preliminary analysis of IFC's performance against these standards during preparation and implementation of the project and in the context of the issues raised by the complainants.

IFC Policy Framework and General Requirements

IFC's investment in the client was made in the context of its 2012 Policy on Environmental and Social Sustainability (the Sustainability Policy) and Performance Standards (PS)—together referred to as the "Sustainability Framework." Through the Sustainability Policy, "*IFC seeks to ensure, through its due diligence, monitoring, and supervision efforts, that the business activities it finances are implemented in accordance with the requirements of the Performance Standards*" (para. 7). The Sustainability Policy also notes that "*central to IFC's development mission are its efforts to carry out investment and advisory activities with the intent to 'do no harm' to people and the environment*" (para. 9). IFC will invest in a project only when the activities it finances "*are expected to meet the requirements of the Performance Standards within a reasonable period of time*" (para 22).

MIGA issued its guarantee covering the project in 2015, after IFC had invested. Therefore, IFC took the primary responsibility for E&S due diligence and project monitoring. As a result, this appraisal focuses on IFC's role, considering that MIGA relied on IFC's pre-investment E&S assessment and supervision of the project.²² In addition to the above policies and standards, IFC's approach to the management of project-related E&S risks is set out in its E&S Review Procedures (ESRP).

Relevant to the specific concerns regarding community safety raised in the complaint, PS4 on Community Health, Safety, and Security establishes requirements for the client to "*evaluate the risks and impacts (of the project) to the health and safety of the Affected Communities during the project life-cycle and ... establish preventive and control measures consistent with good international industry practice (GIIP)...*" (para. 5).

Relevant to the environmental issues raised in the complaint (biodiversity and access to water), PS6 on Biodiversity Conservation and Sustainable Management of Living Natural Resources provides for the assessment and management of impacts on biodiversity. This includes requirements to avoid, minimize and mitigate impacts on "*ecosystem services*" which benefit affected communities (para. 24). In cases where there is a loss of use of or access to "*the products people obtain from ecosystems*" (PS6, para. 2) specific measures are required to ensure livelihood restoration (see PS4, para. 8 and PS5 on Land Acquisition and Involuntary Resettlement, para. 25ff).

Pre-investment Environmental and Social Review

Requirements

As a general requirement, IFC is committed to a pre-investment E&S review that is "*commensurate with the level of environmental and social risks and/or impacts*" (Sustainability Policy, para. 26). IFC's review is required to identify any gaps in the client's practices and propose

²² When the International Finance Corporation (IFC) and/or International Bank for Reconstruction and Development (IBRD) or any World Bank Group (WBG) entity is involved with the project, MIGA may rely on and use such entity's environmental standards, environmental and social due diligence and/or monitoring, in accordance with WBG common or shared guidance. MIGA, Policy on Environmental and Social Sustainability, para 6, October 1, 2013, <https://bit.ly/3EkjFmk>

additional measures and actions to resolve those gaps consistent with IFC requirements. IFC captures supplemental actions in an E&S Action Plan (ESAP) and incorporates them as conditions of IFC's investment (Sustainability Policy, para. 28).

PS 1 (para. 7) requires the client to establish and maintain a process for identifying the environmental and social risks and impacts of the project. The scope of the risks and impacts identification process must be consistent with good international industry practice. The identification process is required to be based on recent environmental and social baseline data at an appropriate level of detail (*Ibid.*). PS1 on the Assessment and Management of Environmental and Social Risks and Impacts also requires that the client implement an environmental and social management system (ESMS) to manage project risks and impacts (para. 13).

Supervision of Environmental and Social Issues

Requirements

Following its approval and investment, IFC monitors the project to ensure compliance with the conditions in the investment agreements and applicable IFC policies and standards (Sustainability Policy para. 7).

PS1 requires that for projects with significant impacts, the client will retain external experts to verify its monitoring information. The extent of monitoring should be commensurate with the project's environmental and social risks and impacts, and with compliance requirements (para. 22).

As set out in the ESRP, "*The purpose of supervision is to obtain information to assess the status of project's compliance with the PS and other specific E&S requirements agreed at commitment; to assess the current level of E&S risk; to provide advice to clients on how to address critical E&S issues; and to identify opportunities for improvement and good practices that could be applied to similar projects.*"²³

The 2012 Sustainability Policy further states that "*if the client fails to comply with its environmental and social commitments as expressed in the legal agreements and associated documents, IFC will work with the client to bring it back into compliance, and if the client fails to reestablish compliance, IFC will exercise its rights and remedies, as appropriate*" (para. 24).

Summary of IFC's General Pre-Investment E&S Review and Supervision

IFC's Environmental and Social Review Summary (ESRS) for the AGL project was disclosed in October 2013.²⁴ The ESRS was based on a joint appraisal mission with EBRD and ADB in May 2013 and an environmental and social (E&S) due diligence report prepared in August 2013 by a third-party consultancy, Arup. IFC and the other lenders visited key project sites and held meetings with various stakeholders, such as local and national non-governmental organizations (NGOs), and the leaders and elders of two affected municipalities and villages.²⁵ The lenders required AGL to prepare Environmental and Social Impact Assessments (ESIAs) to meet

²³ ESRP 6, para.1, version 7, April 15, 2013.

²⁴ IFC Environmental and Social Review Summary, Adjaristsqali Georgia LLC, Project #33435, <https://bit.ly/3lq0av8>

²⁵ *Ibid.*

International Finance Institution (IFI)—including IFC, EBRD and ADB—requirements. The company engaged Mott MacDonald and a local firm, Gamma Scientific, to prepare the ESIA.

Based on the results of this review, IFC classified the project as E&S “Category A²⁶” noting that it had diverse and potentially significant risks and impacts across multiple sites including: hydrology/ecological flow, biodiversity, dam safety and community/worker safety.²⁷ IFC required the client to comply with all of IFC’s Performance Standards with the exception of PS7 on Indigenous Peoples (IPs), since no IPs were identified in the project area.

The ESRS describes IFC’s review of the following documents:

- The project Environmental Impact Assessment (EIA) prepared for Georgian authorities, (2013)
- The ESIA prepared for international lenders (2012 and 2013)
- ESIA Non-Technical Summary (2013)
- Stakeholder engagement plan (2013)
- Environmental and Social Management Plan (ESMP, 2013)
- Biodiversity Action Plan (2013)
- Environmental and Social Due Diligence (ESDD) report developed by ARUP (2013)

The lenders and the client agreed on an Environmental and Social Action Plan (ESAP), which sets out actions to be undertaken by the client during construction and operation of the project. Relevant to the issues raised in the complaint, the client was expected to:

- Report to lenders on the status of each ESAP requirement and compliance with the respective E&S standards (semi-annually during construction and annually during commissioning).
- Finalize development of the Environmental, Social, Health and Safety (ESHS) Management System.
- Identify and evaluate risks to community health and safety from construction and operation of the project, develop and implement commensurate preventive measures and plans to address them (prior to creation of potential risks).

Specific actions included in the ESAP related to biodiversity and groundwater flows are outlined in the subsections that follow.

On May 1, 2014, both investments (equity and loan) were presented to the IFC Board and approved. IFC signed an investment agreement in May 2014. IFC made its first and second equity subscription in November 2014. The first loan disbursement was made in March 2015. MIGA issued a guarantee in April 2015 to Tata Power Company Ltd. for its equity investment in the project.²⁸ Project construction started in June 2014.

²⁶ A Category A project involves “Business activities with potential significant adverse environmental or social risks and/or impacts that are diverse, irreversible, or unprecedented”, <https://bit.ly/31DMdZV>

²⁷ Per IFC’s 2012 Sustainability Policy, a project is categorized A when it involves “*business activities with potential significant adverse environmental or social risks and/or impacts that are diverse, irreversible, or unprecedented.*” (para. 40).

²⁸ Multilateral Investment Guarantee Agency, Adjaristsqali Hydro Project, Project description, <https://bit.ly/3l95tPr>

IFC's supervision of the project consisted of annual visits.²⁹ Its supervision was further informed by Arup reports, with Arup acting as an independent E&S monitoring consultant. Arup also visited the project and reviewed the client's reporting on the project's E&S performance.

During commissioning of the project in 2017, multiple sections of the tunnels collapsed.³⁰ In February 2019, IFC's Board approved a restructuring of the loan, providing necessary funds to assist the client in completing repairs of the collapsed tunnel. In April 2020, IFC sold its share in AGL, thus exiting the equity investment. However, its loan and MIGA's guarantee remained active. The project started operations in March 2020. Due to travel restrictions resulted from COVID-19 in September 2020, the Independent Environmental and Social Consultant (IESC) conducted a virtual mission.

IFC's E&S Review in Relation to Concerns Raised in the Complaint

The following subsections provide an overview of IFC's E&S review in relation to specific issues raised in the complaint: landslides and rockfalls; groundwater flows; and impacts on biodiversity.

1) Landslides and Rockfalls

Pre-investment review

Both the ESIA and the ESRS for the project state that the Adjara region is highly sensitive to natural hazards including mudflows, erosion, and landslides.³¹ The ESIA mentions that more than 250 settlements in the region (around 20,000 households) are in high landslide risk and hazard zones, and that in the last three decades 1,900 houses were destroyed due to landslides. In addition, the ESIA refers to a catastrophic 1989 landslide in the region that buried a small settlement near the village of Skhalta, which is in one of the river valleys affected by the project. The ESIA identifies Shuakhevi municipality in particular as one area at risk of landslides and erosion due to excess farming, high-density of water channels, and deforestation.³² In this context, the ESIA recognizes that any proposed major engineering scheme has the potential to reactivate previous landslides and instigate new ones.³³ The ESIA notes that AGL would determine the project design and future dam site locations based on detailed engineering—geological and topographic—geodetic studies and surveys of the project area in order to locate project infrastructure in areas with minor risks of landslides and erosion, where possible.³⁴ Geomorphological investigations of the Chirukhistsqali weir, located near the Makhalakidzeebi village, determined that the weir site and surrounding slopes had a negligible-to-minor hazard rating and were not considered susceptible to significant landslides. The ESIA also notes that blasting to construct the tunnels close to the surface, and the cuttings for road construction had minor risks of activating landslides.

Mitigating these risks, the ESIA notes that to prevent soil erosion and landslides during road and dam construction, and tunnel excavation, good engineering practice would be followed. This

²⁹ The lenders required the client to submit reports: every six months during construction and annually during operation. Annual site visits were conducted up until the onset of the Coronavirus in 2020.

³⁰ Adjaristsqali Hydropower Project, Semi-annual Environment & Social Monitoring Report (July to December 2017), p.2, <https://bit.ly/32KAXEM>

³¹ IFC Environmental and Social Review Summary, Adjaristsqali Georgia LLC, Project #33435, <https://bit.ly/3lxAWkv>

³² The Makhalakidzeebi Village is located within the Shuakhevi municipality.

³³ Clean Energy Group and Mott MacDonald. ESIA Part II, April 2014. P. 148. <https://bit.ly/3EI3W6m>

³⁴ Geomorphological and landslide maps were included in the ESIA, identifying areas where the risks of landslides ranged from low to high, and where the operation could cause mass movement and impact the scheme and the population, Mott MacDonald and Clean Energy Group. ESIA Part II, April 2014, P. 404. <https://bit.ly/3EI3W6m>

included positioning tunnel portals away from landslide areas, using low energy explosives to minimize shockwaves, and conducting regular visual observation. Further prevention measures for landslides included strengthening water reservoirs, providing concrete screens on the slopes, and excavating through hard rock for the construction of the tunnels.³⁵ In anticipation of the operational phase, the ESIA mentions that a qualified engineering geomorphologist should review the reservoir areas on a bi-annual basis for the first 10 years of operation to confirm that the landslide risk had not changed, for example, due to reservoir level fluctuation.

Supervision

During IFC's supervision, in November 2015, AGL prepared a standalone evaluation of risk on community health and safety and proposed measures to address them. Landslides and flooding caused by planned or unplanned project activities were among the key risks assessed. In addition, the government required AGL to install an online vibration monitoring system in Chanchkhalo in August 2015. AGL installed the system and shared the data with the government.

In February 2016, the IESC reported that selected locations had been monitored for landslides, subject to further investigations as needed. In December 2016, the IESC noted that a joint committee of government officials, communities' representatives, and independent geological experts conducted inspections on houses located along the tunnel alignment prior to, and after, construction of the tunnels in 2014 and 2016. In July 2016, 1,284 houses located in the project area were inspected and compared against the data collected during the August-September 2014 inspection.³⁶ One hundred and twenty-nine houses were identified as damaged due to natural processes not related to the project, and 33 houses were recognized as damaged due to other reasons such as poor foundations and structural defects. The Government of Adjara requested AGL to restore or rebuild the 33 houses because they were located in the area of the project.

In March 2017, IFC reported that there were community protests demanding the installation of landslide monitoring systems and access to geological reports. In response, the IESC required the client to include in the Environmental and Social Management Plan (operations phase) regular observations and maintenance of site access roads. In addition, AGL monitored ground movements through 30 monuments installed within the project area, and no significant change was found in the movement of the ground.³⁷ Later in the year, the client reported ongoing landslide monitoring in Chanchkhalo village as the collapse of the tunnels had created concerns within the local communities there. In this context, AGL conducted several meetings with the communities to explain the issue, remedial actions planned, and how the project would take measures to avoid landslides.

In 2018, the IESC continued to mention that locals attributed landslide activation to tunneling and increased traffic movement. The project grievance mechanism registered 11 complaints regarding erosion and landslides during 2018. However, none of these complaints involved the Makhalakidzebi Village. The IESC reported that AGL did not agree with the allegations but showed willingness to support any road repairs. Periodic site monitoring continued together with tunnel convergence monitoring (post-collapse), and monitoring of specific locations in relation to observations and community requests.

³⁵ Clean Energy Group and Mott MacDonald. ESIA Part III, April 2014. Volume III Appendices. Appendix B. Consultation. B1 Summary of Consultation and Disclosure Activities. October 2012. p. 16. <https://bit.ly/3oefSkS>

³⁶ Semi-annual Environmental and Social Monitoring Report (July to December 2016). Environmental and Social Performance Report. April 2017. <https://bit.ly/31r30Pb>

³⁷ Semi-annual Environment & Social Monitoring Report (January to June 2017). Environmental and Social Performance Report. October 2017. <https://bit.ly/3Dj3LHp>

The IESC visited the site in June 2019 and reported that project had recorded 880 grievances.³⁸ The grievances related primarily to blasting damage to houses and landslide monitoring. AGL also developed a geological monitoring program to be implemented across the commissioning phase so that any geological changes would be identified, and causation established early.

The project commenced commercial operations in March 2020, and in September 2020, the IESC conducted a virtual site visit. AGL reported that in the previous year, the government investigated the tunnel collapse incidents.³⁹ The investigation related to the collapse of a transfer tunnel in August 2017, and the blockades of the head race tunnel in October 2017. In response, AGL de-watered and inspected all the tunnels in the project. Two collapses were visible in the transfer tunnel and several collapses were identified at the head race tunnel due to rockfalls. Tunnel repair works were initiated and AGL's social, environmental, and technical teams worked to address locals' concerns over the tunnel collapse. AGL explained the scale of the blockage required remedial actions and ensured that the blockades would not cause any landslides.⁴⁰

Conclusion

CAO concludes that this issue does not warrant a compliance investigation. Based on a preliminary review of project documentation and interviews with the complainants, it appears that no landslide-related damage occurred in Makhalakidzeebi village during project construction. Project design included attention to geological and topographic studies and maps conducted during pre-appraisal, in addition to the use of low-energy explosives, hard rock excavation, and visual observation as measures to reduce the risk of project-induced landslides. Project supervision included the installation of ground movement monuments, house inspections prior to, and after, construction, and installation of landslide monitoring systems in response to visual observation and communities' requests. In this context— and considering that the complainants indicated to CAO that they did not face major damages to their properties during construction— CAO decided to close this issue.

2) Groundwater Flows

Pre-investment review

The ESIA states that water within the project area is used for irrigation, fish farming and recreational purposes, and such activities were identified as largely unaffected by the project's construction.⁴¹ However, the ESIA also notes that there could be substantial impacts on areas where the tunnel is closest to the surface during construction, including impacts on water resources for drinking, irrigation, and household use. As a result, the ESIA notes that temporary or permanent drainage of water wells could occur with the level of risk or likelihood of occurrence being unknown at that point.⁴² The ESIA recommends mitigation measures in relation to these potential impacts including:

- i. Tunnel lining where there was not a risk of disrupting spring sources used by the rural population.
- ii. Locating construction compounds away from sensitive water features.

³⁸Environmental and Social Monitoring Report (June 2019 site visit). Arup. October 2019. <https://bit.ly/3xRP11k>

³⁹Environmental and Social Monitoring Report (September 2020). Arup. February 2021. <https://bit.ly/3xOax70>

⁴⁰ Semi-annual Environmental and Social Monitoring Report (July to December 2017). Environmental and Social Performance Report. December 2019. <https://bit.ly/3dqOLiW>

⁴¹ Clean Energy Group and Mott MacDonald. ESIA Part II, April 2014. P.392, <https://bit.ly/3DgyULF>

⁴² *Ibid.* P. 148.

- iii. Providing alternative supply systems to the limited number of small-scale irrigators or fish farmers that may be affected.⁴³

The ESIA further notes that potential effects during the operation phase, including the reduction in river flows along the Adjaristsqali River would likely have a direct effect on the aquatic ecosystem and ecosystem services, including impacts on existing water uses for irrigation and household water supply.⁴⁴

IFC's ESRS for the project notes that tunnel alignment was designed to avoid spring water sources used by communities (as noted in the ESIA) and as a result, the risk of water scarcity was relatively low.⁴⁵ Nevertheless, the project would provide temporary water supply in areas where drinking water was lost. Additionally, a permanent alternative water supply would be installed by the project to mitigate the loss of drinking water resources in the long term.

Supervision

During supervision, in August 2014, the IESC visited the project site and reported that to gain the trust of communities, several Memoranda of Understanding (MOU) were signed between local communities' representatives, the municipality, relevant NGOs, and AGL. According to the IESC, the MOUs covered topics such as the quality and quantity of spring water and the quality of local roads. It is not clear from the documentation reviewed whether the IESC or IFC reviewed the MOUs.

In 2015, the IESC visited the project and recommended actions that the client needed to carry out to ensure compliance with the ESAP, including improving the effectiveness and timeliness of its response to communities' grievances related to spring water. The IESC reported that in October, of the previous year, the client was fined by the national authority due to noncompliance with its environmental permit, including inadequacy of spring water monitoring. In response, AGL provided verbal confirmation that a hydrologist was hired to write a monthly assessment of hydrological monitoring and that results were sent to the Georgian Ministry of Environment on a regular basis. However, the IESC also noted that it had not been able to review evidence of the client's actions to address this regulatory compliance issue.

In 2016, the IESC noted that most community grievances were related to reduced or lost spring water. In response, the IESC noted that the client had a functional grievance mechanism in place. However, its management required some improvements. The IESC noted that the client had conducted spring water source monitoring across 20 villages in order to comply with the project's permit. The IESC did not include in its monitoring report any analysis of the spring water monitoring. This, and subsequent IESC reports, do not include any analysis of whether communities' grievances about lost spring water were related to the project. Rather, the issue was dealt with in the context of stakeholder engagement and grievance handling.

In the second half of 2017, project supervision documentation notes that there had been 19 grievances filed to the project complaints mechanism related to loss of spring water. In response, the client explained that these springs were located outside the tunnel alignment and could not have been affected by the project. Nevertheless, AGL undertook water supply projects for some of these villages and the IESC reported that no family was left without water. As a result of a site visit in September 2017, the IESC recommended that the client engage an expert consultant to provide an opinion to lenders about community grievances related to spring water. The IESC would then review the Terms of Reference to hire this consultant. However, it is not clear, based

⁴³ *Ibid.* P 367

⁴⁴ *Ibid.* P. 355

⁴⁵ IFC Environmental and Social Review Summary, Adjaristsqali Georgia LLC, Project #33435, <https://bit.ly/3lxAWkv>

on information available to CAO, whether this assessment of the impacts of the project on spring water was conducted, or what the results were, as it is not referred to in subsequent supervision documentation.

In November 2018, the IESC conducted a site visit and recommended that the client re-initiate spring water monitoring until project operations started.

In 2019, the IESC noted that the client developed a hydrogeological and geological monitoring plan to be implemented during commissioning, with the objective of identifying issues related to the appearance and disappearance of spring waters. At this point, the plan was considered adequate.⁴⁶

In 2020, the IESC described the monitoring of spring waters as rudimentary, as it relied on visual checks by specified AGL personnel.⁴⁷ It recommended the client to: (a) improve hydrogeological monitoring records so that they could be effectively interpreted by third parties; (b) disclose hydrogeological monitoring results to local communities in a meaningful (non-technical) form; and (c) restart participatory spring monitoring.

Conclusion

The ESIA identified substantial potential impacts on the areas where the tunnel is closest to the surface and near the tunnel faces, which could affect water resources for drinking, irrigation, and household use. Prior to investment, IFC noted that because of tunnel alignment, the risk of water scarcity was relatively low. Nevertheless, the project included the provision of water supply in response to temporary or long-term losses of access to water as mitigation measures.

Ongoing community grievances regarding the disappearance and appearance of spring water were raised throughout construction. AGL conducted spring water monitoring during construction as a condition of its environmental permit. Given continuing communities' complaints on this issue, the IESC recommended that the client hire an independent consultant to provide an assessment as to whether the project was impacting water sources. However, it is not clear, from the documentation available to CAO, whether this independent assessment was conducted. Rather, the IESC noted that the client was conducting its own spring water monitoring. As of 2020, this monitoring was described by the EISC as rudimentary. CAO's review of IFC's supervision documentation also raises questions concerning the adequacy of baseline data as would be required to assess project impacts on access to groundwater.

Considering the above, it is not clear that IFC's review and supervision of the project properly considered the question of the project impacts on spring water as relevant to the complainants' village. In particular, CAO has questions as to IFC's review and supervision of PS1 requirements to:

- (a) Assess project risks and impacts following good international industry practice (para. 5)
- (b) Establish environmental and social baseline data at an appropriate level of detail (para. 7), and
- (c) Establish an E&S management program that is commensurate with the project's risks and impacts and responds appropriately to unforeseen circumstances (paras 15 & 16).

⁴⁶ Environmental and Social Monitoring Report (December 2019 site visit). Arup. February 2020. P. 13, <https://bit.ly/3djamqE>

⁴⁷ Environmental and Social Monitoring Report (September 2020 site visit). Arup. February 2021. P. 20, <https://bit.ly/3GpsAnh>

Given the important role that access to spring water has for the complainants' livelihoods, CAO also has questions regarding IFC's application of requirements to mitigate project impacts on ecosystem services following PS4, 5 and 6.

3. Impacts on Biodiversity

Pre-investment Review

The ESIA states that the Adjaristsqali river system is of high biodiversity interest, with a diversity of natural forest habitats and plant, aquatic and terrestrial species. As a result, IFC considered the river basin to be a "critical habitat" as defined in PS6.⁴⁸ The ESIA notes that the project could significantly impact the region's biodiversity and ecosystem services. However, these impacts would be significantly reduced with the implementation of the proposed mitigation measures.⁴⁹

IFC's ESRS states that AGL surveyed the area of the project from 2012 to 2013 covering fish, flora, and other species.⁵⁰ The ESRS notes that impacts on fish and aquatic habitats were anticipated to be most significant as a result of weir and dam wall construction, and changes in flow regimes on the affected rivers during operations. Mitigation measures were proposed in the ESIA and the Environmental and Social Management Plan (ESMP) and consolidated in the Biodiversity Action Plan (BAP) for the project. These include: (a) appointment of a Community Wildlife Officer throughout the project's life cycle, (b) creation of new recreational fishing sites around the reservoirs, and the stocking of reservoirs with native fish species, and (c) planting of mixed-species forest habitats to compensate for habitat lost during project development, among others.

Concerning river flow, the ESRS describes a 10 percent annual mean water flow as the minimum required to maintain a short-term survival habitat for most aquatic biota according to "reputable studies."⁵¹ This was based on the historical use in Georgia and other countries of setting environmental flows at 10 percent of the annual average, often as part of a two-stage system of environmental flow assessment.

The ESRS describes a second stage of environmental flow assessment, the purpose of which is to identify sensitive river reaches and determine reach-specific flow requirements and mitigation, based on ongoing data collection, impact assessment and adaptive management. Following an adaptive management approach, mitigation measures—including habitat enhancement, alteration of the flow regime and offsets—would be considered according to ongoing data collection and consultation with stakeholders, as relevant.

In relation to biodiversity, the ESAP included the implementation of the Biodiversity Action Plan (BAP), including:

- Developing and implementing a detailed monitoring schedule for the evaluation and reporting of ecological impacts, recognizing the findings of additional surveys undertaken prior to construction;

⁴⁸ IFC Environmental and Social Review Summary, Adjaristsqali Georgia LLC, Project #33435, <https://bit.ly/3lxAWkv>

⁴⁹ Clean Energy Group and Mott MacDonald. ESIA Part IV, April 2014. P.43, <https://bit.ly/3dkCZnn>

⁵⁰ IFC Environmental and Social Review Summary, Adjaristsqali Georgia LLC, Project #33435, <https://bit.ly/3lxAWkv>

⁵¹ *Ibid*

- Monitoring upstream and downstream flow of all dams to verify that the required minimum flows are met throughout operation; and
- Undertaking ecological assessments to verify that flows are adequate to preserve biodiversity, or to re-define minimum flows as specified in the BAP throughout construction and operation.

Supervision

In August 2014, the IESC reported that local NGOs were conducting surveys required by the BAP and the EIA. The IESC noted that AGL had appointed a senior environmental officer to ensure the methodological quality of these surveys. These surveys were important to assess whether project construction was impacting biodiversity, and to assess the environmental flows needed to protect biodiversity.

In May 2015, the IESC noted shortcomings in the reporting of the biodiversity surveys conducted by the NGOs. The IESC recommended that the client hire an international biodiversity consultant to monitor the process. The consultant role included: (a) reviewing the surveys and revising the BAP if necessary, (b) ensuring that all BAP actions were being implemented and, (c) associating the findings of the BAP with the project design to ensure that adequate solutions were found. The IESC also reported that the local authorities fined the client due to noncompliance with the environmental permit related. This was specifically regarding environmental flow measurements and delays in submitting required biodiversity and emergency plans. In October 2015, the IESC reported that the client confirmed that an international biodiversity consultant would oversee the BAP.

In March 2016, the IESC noted the client had taken some actions in response to its recommendations on the BAP from the previous supervision report. However, many of the recommendations were still outstanding. The IESC noted again that findings of biodiversity monitoring were insufficient to determine whether proposed minimum flows would achieve acceptable biodiversity impact. The IESC also noted that surveys were not conducted during that year due to inadequate flow conditions. However, the client did not propose alternatives to address this data gap. The IESC recommended the client to confirm that: (a) monitoring survey reports conducted by local consultants were satisfactory; (b) there was no need for further actions as a result of the surveys (c) the design changes were reviewed. The IESC also recommended that the client provide a timeframe for attempts to obtain monitoring data during low-flow conditions in 2016. In March, the lenders sent a letter requesting AGL to act on E&S compliance-related recommendations provided by the IESC since 2015 but not yet actioned. Relevant to biodiversity issues, the lenders required the client to confirm whether the minimum flow proposed would be adequate to minimize impacts on biodiversity during the project's operation, which was expected to start within a year. The client presented a corrective action plan to address this and other E&S compliance issues.

In March 2017, the IESC and the lenders visited the project. The IESC reported that the client had made progress on previous recommendations. However, some actions were still outstanding. The IESC recommended that the client finalize its analysis of how the operational impacts of the project on biodiversity would be managed, as well as finish consolidating the biodiversity monitoring conducted during construction of the project. Later in the year, the lenders and the client agreed on an operational phase ESAP (OESAP). The OESAP included, among other things: (a) developing and implementing a detailed monitoring schedule for evaluation and reporting of ecological impacts and additional surveys undertaken; (b) monitoring and disclosing environmental flow data to demonstrate and verify that required minimum flows were being met;

and (c) conducting ecological assessments to verify that flows were adequate to ensure no net loss of biodiversity, or to redefine minimum flows prior to commencement of operation.

In 2018, the IESC reported that the client made satisfactory progress in the implementation of the BAP. However, the IESC found that the client was only partially compliant with the relevant standards. Relevant to the issues raised in the complaint, the IESC reported that a new international consultant had assumed oversight of BAP implementation—and as mentioned in previous monitoring reports—raised concerns related to deficiencies on how biodiversity monitoring data were reported and analyzed. The IESC recommended that the client ensure the improvement of the 2018 biodiversity data so as to allow the international consultant to conduct a meaningful evaluation and interpretation of the data. This was important to understand trends of the monitored species and therefore understand current impacts on biodiversity in the area of the project. The IESC requested that the client present a plan to improve the quality of the biodiversity monitoring reports.

In June 2019, the IESC visited the project and noted that the client had developed a corrective action plan (CAP) to improve biodiversity monitoring reports and statistical analysis of monitoring data which was being implemented as agreed upon. The objectives of the CAP included: (a) Improving the quality of biodiversity monitoring reports; (b) Implementing an adaptive management approach to biodiversity impacts where possible; and (c) Contracting an independent biodiversity specialist to report annually to the lenders.⁵² The IESC also reported that despite progress, the project was not in compliance with the standards related to pollution prevention and control. This was because the project discharged tunnel waters with highly alkaline pH levels—above national and international thresholds—at a stream in the project area. The IESC required the client to verify impacts and identify remedial and mitigation measures to avoid the occurrence of similar incidents. The IESC noted that this could potentially impact biodiversity, and therefore the client was partially compliant with biodiversity protection and environmental management capacity. The IESC provided recommendations to address these issues.

In February 2020, the IESC reported that AGL assessed the discharge of alkaline tunnel water into the stream and did not find resulting impacts. The IESC further noted that risks of sedimentation from unprotected spoil, close to rivers, remained unaddressed in some areas, since its last supervision visit.

During the virtual mission in September 2020, the IESC noted that the biodiversity trend report conducted by the independent specialist analyzed monitoring data regarding birds, endemic trees, fish, herpetofauna and invertebrates obtained since the start of the project until the end of 2018. The IESC noted a decline in the number of fish species in the Chirukhistsqali River and additional changes in fish abundance at some monitoring locations during the construction period. However, the IESC noted that it was premature to determine whether the decline was due to the project. The IESC concluded that mitigation measures defined in the Operation Biodiversity Action Plan were appropriate and compliant with PS6, but that further monitoring was required to assess changes in the abundance of some species in the longer term. While the IESC found the client to be in full compliance with the applicable standards, it also noted a number of pending actions. For instance, the IESC required that the client demonstrate the status of compliance with the Biodiversity Monitoring Corrective Action Plan. It also required that the client finalize the Operations BAP commitments (including a summary of statistical trend analysis and adopting

⁵² The Corrective Action Plan has two phases: the international consultant would provide training to the NGOs responsible for collecting and reporting data and the consultant would prepare a statistical analysis of the biodiversity monitoring.

mitigation measures informed by this analysis), and that the client proposes a plan for implementing real-time disclosure of e-flows during full operation to the lenders.

Conclusion

The ESIA states that the Adjaristsqali river system is of high biodiversity interest, with a diversity of natural forest habitats, and plants, aquatic and terrestrial species. Mitigation measures were included in the ESAP, including the development and implementation of a BAP, which would be developed in consultation with communities. The project adopted a 10 percent annual mean flow as a minimum environmental flow based on historical usage in Georgia, with a framework for adjustments and the development of additional mitigation measures based on the results of a biodiversity monitoring program.

Starting in 2015, the IESC raised concerns regarding the way the biodiversity monitoring results were being reported. This was important to understand changes in species and assess the project's impacts on biodiversity. It was only in 2019 that the client presented a corrective action plan to address this issue. In the last virtual supervision visit (September 2020), the IESC noted that evidence of compliance with the corrective action plan was still outstanding. A decline in the number of species in the Chirukhistsqali River and changes in fish abundance during the construction period was also reported. While the IESC found it premature to associate these declines with the project, the IESC also states that further monitoring and improvements in the trend analysis were needed to properly resolve the cause of the issue.

Considering the above, it is not clear that IFC's review or supervision of the project was sufficient to ensure compliance with Performance Standard requirements relevant to the complainants' concerns regarding project impacts on biodiversity. In particular, considering that the project impacts critical habitat as defined in PS6, CAO has questions regarding IFC's review and supervision of requirements: (a) to assess project risks and impacts following good international industry practice (PS1, para. 5); (b) to meet stringent requirements for implementing projects in areas of critical habitat (PS6, para. 16); and (c) to ensure project monitoring commensurate with the project's environmental and social risks and impacts (PS1, para. 22 and PS6, para. 17).

IV. CAO Decision

The purpose of a CAO compliance appraisal is to ensure that compliance investigations are initiated only in relation to projects that raise substantial concerns regarding E&S outcomes and/or issues of systemic importance to IFC. In deciding whether to initiate an investigation, CAO weighs factors, including the magnitude of the E&S concerns raised in a complaint, the results of a preliminary review of IFC's E&S performance in relation to these issues, the existence of questions regarding the adequacy of IFC's requirements, and a more general assessment of whether a compliance investigation is the appropriate response in the circumstances.

In this case, the complainants raise concerns regarding the project's current and potential future impacts related to environmental and social issues that are serious in nature. The complainants' concerns regarding the potential for the project to cause landslides and rock falls raise important community safety risks, particularly given the history of landslides in the area. The complainants' allegations that the project has impacted access to groundwater, is of substantial concern given their reliance on spring water for domestic and agricultural use. The complainants' allegations that the project has impacted fish and tree species in what is acknowledged as critical habitat is also of substantial concern given the location of the project and the importance of protecting critical habitat.

This appraisal report has outlined IFC's approach to environmental and social review and supervision of the project. CAO acknowledges measures taken by IFC at appraisal, and during supervision, to ensure project compliance with its E&S requirements. This included review by IFC staff, collaboration with the other lenders, and work with a third-party consultancy responsible for reviewing and monitoring the client's compliance with the ESAP and other lender requirements.

In conclusion, based on a preliminary review of available information, CAO finds that:

- The issues raised by the complainants concerning risks of landslides and rock falls were addressed during IFC's pre-investment and supervision. Given information provided by the complainants to CAO compliance team—that no major damages occurred in their property during project construction, and that the construction phase is over—CAO has decided that this issue does not require an investigation. With respect to concerns raised by complainants regarding groundwater preliminary analysis of the complaint gives rise to questions regarding the adequacy of IFC's E&S review and supervision of the project. This issue is potentially significant in nature considering the complainants' reliance on groundwater for household and agricultural use.
- Preliminary analysis also gives rise to questions regarding the adequacy of IFC's review and supervision of the project related to its impacts on biodiversity. This issue is potentially significant given the designation of the river and the surrounding area as critical habitat as having high biodiversity value.

Taking into consideration all the factors presented above, CAO concludes that a compliance investigation in relation to these issues is warranted.

The Terms of Reference for a compliance investigation in accordance with the CAO Policy are attached in Annex 1.

Annex: Terms of Reference



December 10, 2021
Office of the Compliance Advisor Ombudsman (CAO)

Terms of Reference for Compliance Investigation of IFC and MIGA

*IFC Investment in Adjaristsqali Hydropower Cascade Project
(IFC Projects # 33435, 37781, 601449, 30428; MIGA Project #12315)
Georgia*

About CAO

The Office of the Compliance Advisor Ombudsman (CAO) is an independent recourse and accountability mechanism for the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA). CAO reports directly to the Boards of IFC and MIGA (“the Board”) and is fully independent of IFC/MIGA management.

CAO carries out its work in accordance with the IFC/MIGA Independent Accountability Mechanism (CAO) Policy (“[the CAO Policy](#)”).

CAO’s mandate is to:

- Facilitate the resolution of complaints from people who may be affected by IFC/MIGA projects or sub-projects in a manner that is fair, objective, and constructive
- Enhance the environmental and social outcomes of projects in which those institutions play a role
- Foster public accountability and learning to enhance the environmental and social performance of IFC/MIGA and reduce the risk of harm to people and the environment

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

This document contains the terms of reference for the CAO's investigation of AGL-01, as required by paragraphs 96 and 118 of the CAO Policy.

About CAO's Compliance Function

*"The purpose of the CAO compliance function is to carry out reviews of IFC/MIGA's compliance with E&S [Environmental and Social] Policies, assess related Harm, and recommend remedial actions where appropriate."*⁵³ The compliance function does not evaluate the adequacy or suitability of E&S Policies, nor does it make findings in relation to the compliance of a project, sub-project, client, or sub-client with the IFC Performance Standards. However, in carrying out its role, the CAO compliance function will assess IFC/MIGA's review and supervision of its E&S requirements at the project- or sub-project level and consider project- or sub-project- level environmental and social performance.⁵⁴

CAO's compliance function has three phases:

1. A **compliance appraisal**, which is a preliminary review to determine whether a complaint or internal request merits a compliance investigation.
2. Where warranted, a **compliance investigation**, which is a systematic and objective review to determine whether IFC/MIGA complied with its E&S policies, and whether there is harm related to any IFC/MIGA non-compliance. On completion of a compliance investigation leading to findings of non-compliance and related harm, CAO makes recommendations for IFC/MIGA to consider when preparing its Management Action Plan (MAP). IFC/MIGA submits the MAP to the Board for approval.
3. Where there is an approved MAP, CAO will conduct a **compliance monitoring** process and report on the effective implementation of any corrective measures included in the MAP.

The Investment

The Shuakhevi project, is a 184 MW hydropower scheme located in the Adjara region in the southwest Georgia implemented by AGL. It comprises of two dams, reservoirs, a weir, underground tunnels, new roads, and bridges. Total project cost was estimated to be US\$427 million. Project construction began in June 2014 and, the project started operation in March 2020.

The investment was supported by senior loans from IFC, EBRD and ADB. IFC's investment consisted of an A loan of up to US\$71 million and equity of up to US\$34 million. IFC also had an Advisory Services project to advise on AGL's retrenchment strategy. In addition, MIGA provided a \$63 million guarantee to Tata Power International Pte. Ltd. to cover its equity investment in the Project. In December 2016, IFC completed its advisory services engagement with AGL, and in April 2020 IFC sold its share in AGL thus exiting the equity investment. IFC's A loan and MIGA's guarantee projects remain active.

⁵³ CAO Policy, Sec. X, para. 76.

⁵⁴ CAO Policy, Sec. X, para. 77.

The Complaint

In February 2018, CAO received a complaint from 22 households in Makhalakidzeebi village, Shuakhevi Municipality, Adjara, Georgia, located less than 500 meters from one of the project tunnels. The complaint alleges several current and potential negative impacts to the residents of Makhalakidzeebi and the local environment as a result of the project's construction and operation. The complaint includes the following topics: landslides and rockfalls, groundwater flows, and impacts on biodiversity.

Investigation Terms of Reference

Where an appraisal process results in a decision to investigate, as in this case, CAO's appraisal report includes terms of reference for the compliance investigation, outlining:

- a) *The objectives and scope of the investigation*
- b) *Any limitations on the scope of the investigation that may be appropriate, considering, among others, issues closed at the appraisal stage, the presence of concurrent judicial proceedings, or an IFC/MIGA Exit*
- c) *The approach and method of investigation, and specific consultant qualifications*
- d) *A schedule for the investigation tasks, timeframe, and reporting requirements. This schedule will include deadlines for the submission of information by IFC/MIGA to inform the compliance investigation process.*⁵⁵

A. Objective, Scope, and Methodological Approach

Objective and Scope: As established in CAO's appraisal report, CAO will conduct a compliance investigation of IFC's investment in the Shuakhevi project in relation to two issues raised in the AGL-01 complaint: groundwater flows and impacts on biodiversity.⁵⁶

In relation to these issues, the objective of the investigation is to determine:

1. Whether IFC/MIGA has complied with its E&S Policies, including:
 - a. Whether IFC/MIGA has materially deviated from relevant directives and procedures
 - b. How IFC/MIGA reviewed and supervised the Project's compliance with its E&S requirements, including applicable national law where relevant to IFC/MIGA E&S requirements
2. Whether there is harm or potential harm related to any IFC/MIGA non-compliance.⁵⁷

The investigation will focus on IFC/MIGA's due diligence and supervision of AGL with respect to the assessment, prevention, and mitigation of project impacts on groundwater flows and biodiversity. Specifically, it will examine whether IFC obtained information necessary to assess the status of the project's compliance with IFC's 2012 Policy on Environmental and Social Sustainability and the Performance Standards. It will also examine whether IFC assured itself of the client's capacity and commitment to implement the requirements of Performance Standard (PS) 1 on the Assessment and Management of Environmental and Social Risks and Impacts, PS4 on Community Health, Safety, and Security, and PS6 on Biodiversity Conservation and

⁵⁵ CAO Policy, Sec. X, para. 118.

⁵⁶ While the complaint also raised concerns regarding landslides and rockfalls, the issue was closed at compliance appraisal. Please refer to the CAO compliance Appraisal Report for more information.

⁵⁷ CAO Policy, Sec. X, paras. 112 - 114.

Sustainable Management of Living Natural Resources as relevant to potential project impacts on groundwater and biodiversity in light of the project context and scale, and good international industry practice (GIIP).

CAO's compliance function does not make findings in relation to compliance of a project, sub-project, client, or sub-client with the Performance Standards. However, in making findings regarding harm and whether any harm is related to IFC/MIGA non-compliance with their E&S Policies, CAO will assess, as relevant, IFC/MIGA's review and supervision of its E&S Requirements at the project- or sub-project-level, and consider project- or sub-project-level E&S performance.

Methodological Approach: CAO will base the compliance investigation on information made available to CAO from interviews, statements, reports, and correspondence, as well as CAO observations of activities and conditions at the project site, and other information sources that CAO deems relevant.⁵⁸

The compliance investigation process and investigation report will include:

- a. *The investigation findings with respect to compliance, non-compliance, and any related harm.*
- b. *Context, evidence, and reasoning to support CAO's findings and conclusions regarding the underlying causes of any non-compliance identified.*
- c. *Recommendations for IFC/MIGA to consider in the development of a Management Action Plan (MAP) relating to the remediation of project- or sub-project-level non-compliance and related harm, and/or steps needed to prevent future non-compliance, as relevant in the circumstances. In case of a project where the IFC/MIGA exit has occurred, recommendations will take into account the implications of such an IFC/MIGA exit.*⁵⁹

Sufficient, relevant evidence is required to afford a reasonable basis for CAO's compliance findings and conclusions. CAO will assess whether there is evidence that IFC/MIGA applied relevant E&S requirements considering the sources of information available at the time the decisions were made and will not make findings and conclusions with the benefit of hindsight.⁶⁰

External Experts:

To assist with this compliance investigation, CAO will engage one or more external experts in groundwater flows and riverine biodiversity with the following qualifications:

Groundwater Expert:

- Significant expertise and experience in groundwater flows, particularly in the context of hydroelectric projects.
- Significant expertise and experience in risk assessment and management of potential impacts on groundwater flows in the context of hydroelectric projects involving tunneling activities.

⁵⁸ CAO Policy, Sec. X, paras. 115 and 117.

⁵⁹ CAO Policy, Sec. X, para. 120.

⁶⁰ CAO Policy, Sec. X, paras. 116 - 117.

- Knowledge of relevant IFC standards and sources of Good International Industry Practice
- Experience working in Georgia, and knowledge of relevant national legal requirements would be an asset.

Biodiversity Expert:

- Significant expertise and experience in: assessing risks and potential impacts to riverine biodiversity, designing and implementing preventive and mitigating measures to protect biodiversity, particularly in the context of hydroelectric projects.
- Knowledge of relevant IFC standards and sources of Good International Industry Practice.
- Experience working in Georgia, and knowledge of relevant national legal requirements would be an asset

Field Visit:

A field visit to the Shuakhevi project area and the Makhalakidzebi village is anticipated during the compliance investigation stage, COVID-19 travel restrictions permitting. For such a visit, the CAO case team, external experts, and a translator/interpreter would be expected to participate.

B. Compliance Investigation Schedule, Timeframe, and Reporting Requirements

In accordance with the CAO Policy⁶¹, a draft compliance investigation report must be circulated within one year of the disclosure of an appraisal report. By December 2022, a draft compliance investigation report for this case will be circulated to IFC/MIGA management and all relevant IFC/MIGA departments for factual review and comment. Management may share the draft report with the client or sub-client on the condition that appropriate measures are in place to safeguard the confidentiality of the draft report prior to disclosure.⁶²

Applying appropriate measures to safeguard the draft report’s confidentiality prior to disclosure, the draft investigation report will be circulated to the complainants for their factual review and comment at the same time. If such confidentiality measures are not in place, complainants will, at a minimum, receive a draft table of the investigation’s findings for factual review and comment and as a source of information to inform future consultations on any IFC/MIGA Management Action Plan (MAP).⁶³

The period for IFC/MIGA’s factual review and comment is 20 business days. Upon receiving comments on the consultation draft from IFC/MIGA and the complainants, CAO will finalize the investigation report. The final report will be submitted to IFC/MIGA senior management and circulated to the Board for information. The Board has no editorial input on the content of a CAO compliance investigation report. Once the investigation report is officially submitted to IFC/MIGA management and circulated to the Board, CAO will notify the public on its website of the investigation’s completion.⁶⁴

⁶¹ CAO Policy Sec. X, para 121

⁶² CAO Policy, Sec. X, para 122.

⁶³ CAO Policy, Sec. X, paras. 124 - 125.

⁶⁴ CAO Policy, Sec. X, paras. 123 and 127 - 129.

Upon CAO's official submission of the compliance investigation report to IFC/MIGA, IFC/MIGA management has 50 business days to submit a management report to the Board for consideration. The management report must include a MAP for Board approval. A MAP contains time-bound remedial actions that IFC/MIGA proposes for the purpose of addressing CAO findings of non-compliance and related harm. IFC/MIGA must consult with complainants and the client during its MAP preparation process, and its management report must also include a reasoned response to CAO's finding or recommendations regarding non-compliance or related harm that IFC/MIGA is unable to address in the MAP.⁶⁵

CAO will submit comments on the proposed MAP to the Board, and the complainants may submit a statement to CAO on the proposed MAP and the adequacy of consultations for circulation to the Board.⁶⁶ Upon the Board's approval of the MAP, the compliance investigation report, management report, and MAP will be published on CAO's website.⁶⁷

⁶⁵ CAO Policy, Sec. X, paras. 130 - 132 and 134.

⁶⁶ CAO Policy, Sec. X, para. 135.

⁶⁷ CAO Policy, Sec. X, para. 138.