



January 21, 2022
Office of the Compliance Advisor Ombudsman (CAO)

COMPLIANCE APPRAISAL

Karot Hydro, Pakistan (IFC Project # 34062 and # 36008)

Complaint Karot-02 & 03/Jhelum River

Table of Contents

Executive Summary	3
About CAO.....	7
Acronyms.....	8
1. Overview of the Compliance Appraisal Process.....	9
2. Background	10
2.1. IFC Investment	10
2.2. Karot-02 and Karot-03– The Complaints and CAO Assessment	11
3. Analysis	12
3.1. IFC Policy Framework and Requirements.....	12
3.2 IFC’s Pre-Investment E&S Due Diligence	13
3.3 IFC Supervision	16
4. CAO Decision	18
Annex A: Perspective of Karot-02 complainant and Company on raised concerns (from CAO Assessment Report).....	21
Annex B: Perspective of Karot-03 complainants and Company on raised concerns (from CAO Assessment Report).....	23
Annex C: Terms of Reference for Karot 02-03 Investigation.....	26

Executive Summary

Karot Power Company Limited (“KPCL”, “the Company”, “the client”) is constructing a 720-megawatt run-of-the-river hydropower plant (the “Karot project”) on the Jhelum River, Pakistan. In November 2014, IFC made an equity investment in China Three Gorges South Asia Investment Limited (CSAIL), the parent company of KPCL. In November 2016, IFC committed to a US\$100 million loan to KPCL to support the Karot project specifically. Project construction commenced in January 2016 and it is expected to be complete by April 2022. During construction, the Karot Project has employed up to 5,600 workers, mostly Chinese and Pakistani nationals.

In August 2019, CAO received a complaint (the Karot-02 complaint) from a former worker at the project. The Karot-02 complaint raises both individual labor related concerns and concerns which are systemic in nature. The individual concerns involve allegations of unfair dismissal and incorrect payment of wages upon termination. The broader concerns raised in the Karot-02 complaint include allegations that the project discriminates between local Pakistani and Chinese workers, specifically in relation to access to drinking water, conditions of accommodation, and access to transportation at the project site.

In July 2020, CAO received an additional complaint (the Karot-03 complaint) from representatives of Building and Wood Workers International (BWI) and the Pakistan Federation of Building and Wood Workers (PFBWW). The complaint was submitted on behalf of the Awami Labor Union (ALU) at the Karot Power Company Limited. The complaint alleges adverse project impacts on approximately 3,000 Pakistani workers at Karot. Specifically, the Karot-03 complainants raise concerns regarding: (i) Company interference in union activities; (ii) poor Occupational Health and Safety (OHS) conditions, including Covid-19 procedures; (iii) low wages and poor retrenchment practices; (iv) a lack of effective complaints handling processes for workers; and (v) the presence of security personnel creating an intimidating atmosphere that impacts workers’ ability to participate in union activities.

The Karot-02 complaint was transferred to CAO’s compliance function in December 2020 after the complainant ceased communication with CAO. The Karot-03 complainant was transferred to CAO’s compliance function in April 2021 as the parties did not agree to a CAO facilitated dispute resolution process.

Following transitional arrangements agreed as part of the CAO Policy process, CAO’s 2013 Operational Guidelines govern this compliance appraisal. Applying the Operational Guidelines, the purpose of a CAO compliance appraisal is to ensure that compliance investigations are initiated for those projects that raise substantial concerns about environmental and/or social (E&S) outcomes, and/or issues of systemic importance to IFC/MIGA.

IFC’s pre-investment E&S due diligence for the project was conducted between 2014 and 2016. IFC is required to conduct E&S due diligence at a level that is commensurate with the nature, scale, and stage of the business activity, and with its level of E&S risks and impacts. IFC will only finance projects that can be expected to meet the requirements of its E&S Performance Standards (PS) within a reasonable period of time. The issues raised in the complaint are specifically relevant to the implementation of IFC PS2 (Labor and Working Conditions) and PS4 (Community Health, Safety and Security).

IFC’s E&S due diligence for the Karot project resulted in a determination that the E&S risk of the Karot project was Category A, meaning that it involved potential significant adverse E&S risks and/or impacts that are diverse, irreversible, or unprecedented.

At the time IFC initiated its E&S due diligence, construction of the project had not commenced. IFC E&S staff held meetings with Company in China and Pakistan. The Company only had a small workforce of approximately 50 at this point and didn't yet have human resources procedures. As a result, IFC did not review the Company's labor related policies or performance. Rather, IFC sought to assure itself that the Company would manage its construction workforce in a manner consistent with the Performance Standards, by including a number of broad commitments in the project E&S Action Plan. These included a commitment for the Company to provide for IFC's review and approval a Contractor Management Plan, inclusive of a plan for monitoring the performance of the construction contractor's environmental, social, health, safety and social management (ESHS) performance and other labor related items in the ESAP. The labor related actions in the ESAP were initially due for completion before the end of 2015, however, these deadlines were extended to August 2016.

In April 2016, prior to approval of IFC's investment in the Karot project, IFC staff conducted a site visit. At this point, construction activity at the project site had been underway for three months and it was expected to ramp up further over the next three months. IFC noted that the Company's management plans with the project's construction contractor were fit for purpose, though some remained to be reviewed by IFC. However, IFC also identified apparently serious OHS concerns at the construction site. These included: (i) insufficient communication of OHS requirements from project management to project level staff; (ii) a lack of relevant supervisory staff; (iii) inconsistent use of worker personal protective equipment; and (iv) insufficient training of new hires on OHS or job training.

IFC's Board approved the investment in May 2016 and IFC legally committed its loan to the project in November 2016. Prior to these events, based on a review of available documentation, it is unclear to CAO whether IFC took sufficient steps to assure itself that the client was on track to meet the labor related commitments set out in the project ESAP. It is similarly unclear, whether IFC had verified that the client was addressing the on-site OHS concerns that IFC had identified during its April site visit.

Following commitment of a loan, IFC is required to supervise the client to ensure compliance with the Performance Standards and other specific E&S requirements agreed as conditions of investment. If a client fails to comply with its E&S commitments, IFC is required to work with the client to bring it back to compliance, and if the client fails to reestablish compliance, IFC is required to exercise remedies as appropriate. Based on documentation provided by IFC, CAO's compliance appraisal has reviewed IFC's supervision activity up to April 2021.

Over the course of IFC's investment in the project, IFC became aware of a range of concerns related to labor, working conditions and OHS at the project site. In response to supervision observations and subsequent complaints from workers, IFC enhanced its supervision of labor issues and commissioned specialized labor assessments in late 2019 and 2021. The labor assessments confirmed gaps in the project's handling of labor issues and led to the development of corrective action plans.

While IFC's supervision has documented improvements in client performance in response to corrective action plans agreed with the client, based on CAO's preliminary review of IFC supervision documentation there are indications that concerns raised in the complaint, including poor living conditions in worker accommodations, poor workplace safety practices, discrimination between Chinese and Pakistani workers, and limitations on freedom of association, have persisted through the life of IFC's investment.

Decision

Under the 2013 Operational Guidelines, the purpose of a CAO compliance appraisal is to ensure that compliance investigations are initiated 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 takes into account the following criteria in determining whether it is appropriate to initiate a compliance investigation in response to a complaint:

- Whether there is evidence of potentially significant adverse environmental and/or social outcome(s) now, or in the future (Criteria 1)
- Whether there are indications that a policy or other appraisal criteria may not have been adhered to or properly applied by IFC/MIGA (Criteria 2)
- Whether 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 (Criteria 3).

In this case CAO has made a decision to investigate based on criteria 1 and 2.

Evidence of potentially significant adverse environmental and/or social outcome(s) now, or in the future

IFC project documentation identified substandard living conditions in worker accommodations, poor workplace safety practices, discrimination between Chinese and Pakistani workers, and limitations on freedom of association that are consistent with those raised by the complainants. While these issues were picked up through IFC supervision, it is not clear that they were resolved in compliance with IFC standards during the 6-year construction period of the project. In the context of a large construction project with significant E&S risks and impacts, CAO's preliminary review of IFC supervision documentation and other available evidence indicates potentially significant adverse impacts on workers, specifically in relation to worker health and safety as well as workers' ability to organize.

Indications that a policy or other appraisal criteria may not have been adhered to or properly applied by IFC/MIGA

CAO acknowledges that the IFC has taken measures to improve the client's labor management performance. Nevertheless, CAO's preliminary review has found indications that IFC may not have complied with its policy requirements related to the issues raised in the complaints. These include:

- i. There is a lack of documented analysis of the client's labor related management plans during IFC's pre-investment review of the project.
- ii. There is a lack of documented assessment of client and contractor capacity to manage complex labor and OHS aspects of the project to IFC standards prior to investment.
- iii. There is a lack of clarity as to how IFC addressed serious on-site OHS concerns that were identified during a pre-investment site visit.
- iv. Labor and OHS compliance issues identified by IFC and external consultants have persisted throughout the construction period of the project.

In this context, CAO has decided to conduct a compliance investigation into the following labor issues raised by the Karot-02 and 03 complaints: (a) discrimination in the provision of worker services; (b) freedom of association; (c) workplace health and safety; (d) wage and retrenchment practice; (e) worker grievance handling; and (f) project security arrangements. In addition to addressing the specific concerns regarding adverse impacts raised by the Karot construction workers, CAO finds value in a compliance investigation in this case, given IFC's ongoing equity exposure to the parent company. This provides an opportunity for lessons from Karot to be integrated into IFC's supervision of any future CSAIL construction projects.

CAO has, however, decided not to conduct a compliance investigation in relation to the individual (unfair dismissal and payment) concerns raised in the Karot-02 complaint. As noted in previous CAO compliance appraisals, disputes between an employer and an individual employee that relate to working conditions or terms of employment do not usually raise substantial concerns regarding the E&S outcomes of a project which necessitate a CAO investigation.

Terms of Reference for this investigation are presented in Annex C.

About CAO

The Office of the Compliance Advisor Ombudsman (CAO) is an independent recourse and accountability mechanism that receives complaints from communities and persons who may be affected by the projects that the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA) support. The 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 complementary 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.¹ The CAO compliance function follows a three-step approach: (1) compliance appraisal, which determines whether further investigation is warranted. If warranted, the appraisal is followed by (2) compliance investigation and (3) compliance monitoring.²

Following transitional arrangements agreed as part of the CAO Policy process, this compliance appraisal report was prepared following CAO’s 2013 [Operational Guidelines](#).³

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

¹ IFC/MIGA Independent Accountability Mechanism (CAO) Policy, para. 76.

² Ibid, para. 79.

³ CAO Transitional Arrangements were published in July 2021 and are available at <https://bit.ly/3wSnue3>.

Acronyms

Acronym	Definition
ALU	Awami Labor Union
BWI	Building and Wood Workers International
CAO	Office of the Compliance Advisor Ombudsman (IFC and MIGA)
CPEC	China-Pakistan Economic Corridor
CSAIL	China Three Gorges South Asia Investment Limited
CTGC	China Three Gorges Corporation
CTGI	China Three Gorges Investments
E&S	Environmental and Social
EOBI	Employees Old-Age Benefits Institution
EPC	Engineering, procurement, and construction contractors
ESAP	Environmental and Social Action Plan
ESMP	Environmental and Social Management Plan
ESMS	Environmental and Social Management System
ESRS	Environmental and Social Review Summary
ESRP	Environmental and Social Review Procedures
FTA	Finance Technical Advisor
FoA	Freedom of Association
GN	Guidance Notes
GoP	Government of Pakistan
GRM	Grievance Redressal Mechanism
HPP	Hydropower Plant
HR	Human Resources
HSE	Health, Safety and Environment
IESC	Independent Environmental and Social Consultant
IFC	International Finance Corporation
KPCL	Karot Power Company Limited
MIGA	Multilateral Investment Guarantee Agency
NSDWQ	National Standards for Drinking Water Quality
OHS	Occupational Health and Safety
PESSI	Punjab Employees Social Security Institution
PPE	Personal Protective Equipment
PFBWW	Pakistan Federation of Building and Wood Workers
PS	Performance Standards (IFC)
PS2	Performance Standard 2
PS4	Performance Standard 4
SSV	Site Supervision Visit
TGDC	Three Gorges Technology and Economy Development Co., Ltd
WCMC	Workers' Council and Management Committee

1. Overview of the Compliance Appraisal Process

As noted above, following transitional arrangements agreed as part of the CAO Policy process in 2021,⁴ 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 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.

The focus of the CAO compliance function is on IFC and MIGA, not their client. CAO assesses how IFC/MIGA assured itself/themselves of the environmental and social performance of its business activity if finances or advice provided to a client, 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 policy 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 holds discussions 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.

⁴ IFC/MIGA Independent Accountability Mechanism (CAO) Policy Transitional Arrangements, available at: <https://bit.ly/3wSnue3>

2. Background

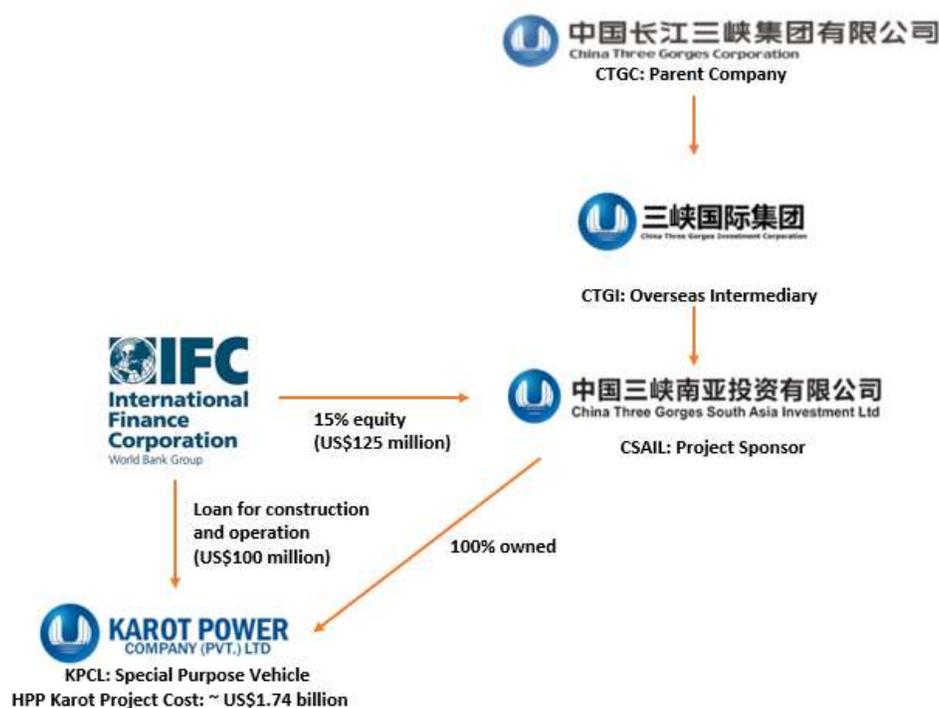
This section presents a summary of IFC's financial exposure to the Karot project, a large hydropower plant under construction in Pakistan. Thereafter, it presents a summary of the complaints to CAO in relation to this project.

2.1. IFC Investment

In November 2014, IFC committed to a 15 percent equity investment for US\$125 million in China Three Gorges South Asia Investment Limited (CSAIL, or "the project sponsor"). CSAIL was established to develop renewable power generation projects in Pakistan and other parts of south Asia.⁵ CSAIL was established by China Three Gorges Corporation (CTGC) through a wholly-owned overseas investment company, China Three Gorges Investments (CTGI).

In May 2016, IFC approved a US\$100 million loan to finance the construction, operation, and maintenance of a 720MW run-of-the-river hydropower plant (the "Karot project") on the Jhelum River, Pakistan, by Karot Power Company Limited ("KPCL", "the Company", or "the client") - a special purpose vehicle that is majority owned by CSAIL.⁶ The figure below describes IFC's exposure to the Karot project.

Figure 1: IFC's Exposure to the Karot Hydropower Project



⁵ IFC Project #34062 Information: China Three Gorges South Asia Investment Limited. Available at <https://bit.ly/3eD2UYz>.

⁶ IFC Project #36008 Information: Karot Hydro Summary of Investment Information - <https://bit.ly/2V0OcDH>.

Given IFC's direct exposure to the Karot project, this compliance appraisal focuses on IFC's loan to the project owner, KPCL, rather than IFC's equity holding in the parent company, CSAIL.

The total cost for the Karot project is estimated at US\$1.74 billion.⁷ Project construction commenced in 2016. IFC's first loan disbursement for the Karot project was made in April 2017.⁸ Construction of the project is expected to be complete by April 2022.⁹

IFC categorized the environmental and social (E&S) risk of the Karot project as Category A. This indicated that the project was expected to involve potential significant adverse environmental or social risks and/or impacts that are diverse, irreversible, or unprecedented.¹⁰

According to IFC, during the peak of construction, Karot was expected to employ nearly 3,500 workers, estimating 85% of the construction workforce to be Pakistani.¹¹ The main engineering, and construction contractor on the project is Yangtze Three Gorges Technology and Economy Development Co., Ltd. (TGDC) and China Machinery Engineering Corporation (CMEC) is the equipment procurement contractor (collectively EPC contractors). TGDC is a wholly owned subsidiary of CTGC.¹²

2.2. Karot-02 and Karot-03– The Complaints and CAO Assessment

Karot-02^{13, 14}

In August 2019, CAO received a complaint from a former worker of TGDC, a project contractor. The Karot-02 complaint alleges that:

- i) the complainant was unfairly dismissed and wages due were withheld upon termination; and
- ii) the project contractor discriminated against local Pakistani workers as compared to Chinese workers in relation to provision of services on the project site. In particular, the complaint alleges that Pakistani workers have substandard access to drinking water, conditions of accommodation, and access to transportation at the project site.

The complainant also mentioned concerns raised by other Pakistani employees about their terms of employment, specifically in relation to workers being unfairly terminated, being employed without contracts, and not receiving adequate salaries for their qualifications.

During CAO's initial assessment of the Karot-02 complaint, the complainant ceased communication with CAO. CAO made multiple attempts to re-establish communication and advance the assessment process, however, these attempts were unsuccessful. Since a CAO dispute resolution process requires voluntary agreement to participate by the complainant(s) and the company, and the complainant ceased communication with CAO, the case was transferred

⁷ 20 percent equity (US\$400 million) and 80 percent debt (US\$1,600 million). IFC investment is for up to US\$100 million A Loan. IFC Project Information and Data Portal: Karot Hydro. Available at: <https://bit.ly/2V0OcDH>.

⁸ IFC Project Information: Karot Hydro Summary of Investment Information - <https://bit.ly/2V0OcDH>.

⁹ News and Media. Karot Power Company Limited, May 18th, 2021. Available at: <https://bit.ly/3ld6coT>.

¹⁰ Per IFC's 2012 Sustainability Policy, para. 40.

¹¹ IFC project documentation indicates that the total workforce at one point was 5,600 workers.

¹² IFC E&S Review Summary, PN 36008, available at <https://bit.ly/3rkE4Sq>.

¹³ In March 2019, CAO received a Karot-01 complaint raising similar labor issues to the ones raised in Karot-02 and Karot-03. The complaint was determined ineligible as it was submitted anonymously.

¹⁴ In March 2019, CAO received its first complaint (Karot-01) in relation to the Karot project. CAO determined this complaint ineligible on the basis that the complaint was anonymous. CAO's Operational Guidelines (2013) stipulate that CAO cannot accept an anonymous complaint (para. 1.4).

from assessment directly to CAO's compliance function in December 2020, for appraisal in accordance with CAO's Operational Guidelines.¹⁵

Karot-03

A further complaint about the Karot project was filed with CAO in July 2020 by representatives of Building and Wood Workers International (BWI) and the Pakistan Federation of Building and Wood Workers (PFBWW). PFBWW is the BWI affiliated union in Pakistan.¹⁶ The complaint was submitted on behalf of the Awami Labor Union (ALU) at the Karot Power Company Limited. ALU is an enterprise union affiliated with PFBWW.

The complaint raises concerns about adverse project impacts on approximately 3,000 Pakistani workers at Karot. Specifically, the Karot-03 complaint makes the following allegations;

- i) *Freedom of Association*. The company has interfered in the establishment and operation of a workers' organization (union);
- ii) *Worker's health and safety*. The company has not provided adequate personal protective equipment to workers or implemented appropriate Covid-19 procedures leading to unsafe conditions;
- iii) *Terms of employment and retrenchment*. Wage levels are below comparative industries in Pakistan, benefits required under Pakistan law are not provided, and workers are dismissed without justification or compensation;
- iv) *A workers' grievance mechanism* has not been established at the project site; and
- v) *Security personnel*. It is alleged that the presence of security personnel creates an intimidating atmosphere that impacts workers' ability to freely exercise their rights in the collective bargaining process.¹⁷

During CAO's assessment, the parties did not agree to a CAO facilitated dispute resolution process. As a result, the complaint was referred to CAO's compliance function for appraisal in April 2021.

The perspectives of the complainants and the client on these issues, as set out in CAO's Assessment Reports for Karot-02 and 03, are summarized in Annexes A and B. Given the similarities of issues raised in the two complaints, CAO has decided to merge the two cases for this compliance appraisal.

3. Analysis

This section outlines IFC's E&S policies and procedures as they apply to this investment. It then provides a preliminary analysis of IFC's performance against these standards during pre-investment due diligence and supervision of the project in the context of the issues raised by the complainant.

3.1. IFC Policy Framework and Requirements

IFC's investment in the project 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

¹⁵ CAO, Karot Hydro-02/Jhelum Assessment Report, November 2020 - <https://bit.ly/3b9JAS2>.

¹⁶ BWI is a global union federation that establishes unions with members of the building, building materials, wood, forestry, and allied sectors. BWI's website: <https://www.bwint.org/>

¹⁷ CAO, Karot Hydro-03/ Jhelum River Assessment Report, March 2021. Available at <https://bit.ly/3hQVlzB>.

it finances are implemented in accordance with the requirements of the Performance Standards”. Central to IFC’s investment activities is an intent to “do no harm” to the people and the environment and to achieve positive development outcomes. The Performance Standards are E&S standards that IFC requires its clients to follow throughout the life of an IFC investment. These standards are supplemented by detailed Guidance Notes, Toolkits, and Handbooks which provide additional requirements and guidance on implementation.

Relevant to the issues raised in the complaints case, the table below summarizes Performance Standard 2 and 4 requirements which an IFC client must follow.¹⁸

IFC Performance Standard 2: Labor and Working Conditions	
Working Conditions and Management of Worker Relationship	Adopt and implement human resources policies and procedures appropriate to its size and workforce
	Provide reasonable working conditions and terms of employment
	Implement policies on the quality and management of the accommodation and provision of basic services
	Where national law recognizes unionization, comply and recognize workers’ rights to form and to join workers’ organizations of their choosing without interference. Do not favor one workers’ organization over another or retaliate against workers
	Discrimination on the basis of race, nationality, or ethnicity is not permitted
	For retrenchment, comply with legal and contractual requirements for worker consultation, notice and severance payment
	Implement a grievance mechanism that is easily accessible and addresses complaints in a prompt and transparent manner
Occupational Health and Safety	Provide a safe and healthy work environment including taking steps to prevent accidents, injury, and disease occurring in the course of work
IFC Performance Standard 4: Community, Health, Safety, and Security	
Security Personnel	Assess risk posed by security arrangements, and train security forces on appropriate use of force and conduct towards workers
	Where government security personnel are deployed to project site, assess risk and request government security personnel act in a manner consistent with PS4.

3.2 IFC’s Pre-Investment E&S Due Diligence

This section summarizes IFC’s pre-investment E&S requirements and IFC’s E&S due diligence for the Karot project leading to preliminary conclusions on IFC’s performance in relation to the issues raised in complaints.

IFC Pre-investment E&S Due Diligence Requirements

At the pre-investment stage, IFC reviews the E&S risks and impacts of a proposed investment and agrees with the client on measures to mitigate these risks in accordance with the Performance Standards. IFC’s pre-investment due diligence is required to be “commensurate with the nature, scale, and stage of the business activity, and with the level of environmental and social risks and impacts.”¹⁹ This includes consideration of “all available information” about project risks and impacts as well as the capacity, maturity, and reliability of the client’s E&S corporate management

¹⁸ Table prepared on the basis of PS2 and PS4 requirements.

¹⁹ IFC 2012 Sustainability Policy, para. 26.

system.²⁰ Where possible, as a measure of the client's management system effectiveness the pre-investment due diligence will also consider projects the client has previously developed and is currently undertaking. Where IFC identifies gaps in the client's systems or performance against its E&S requirements, IFC agrees on an E&S Action Plan (ESAP) with the client as requirement of IFC's investment.²¹ The Sustainability Policy provides that "IFC will only finance investment activities that are expected to meet the requirements of the Performance Standards within a reasonable period of time".²² Thus, the due diligence process leads to a determination of whether the business activity IFC finances are expected to meet the requirements of the Performance Standards within a reasonable period of time.

IFC Pre-investment E&S Due Diligence of the Karot Project

IFC commenced its pre-investment due diligence for the Karot project in the second half of 2014. IFC disclosed its proposed investment in the project in April 2015. Construction commenced in January 2016. IFC conducted a visit to the project site in April 2016, prior to IFC Board approval in May 2016. In November 2016, IFC signed the loan agreement with KPCL, contractually committing IFC to financing the project.

As set out in its investment disclosures (Environmental and Social Review Summary - ESRS), IFC reviewed all E&S studies and documents prepared for the Karot project including an environmental and social impact assessment (ESIA) which was conducted in July 2015 which includes an environmental and social management plan (ESMP). In August 2015, IFC disclosed the Environmental and Social Action Plan (ESAP) agreed with KPCL for the Karot project which outlines actions to address the identified gaps in the Karot as required for the project to comply with IFC's Performance Standards.

At the time of IFC's pre-investment E&S due diligence, the Company only had a small workforce of approximately 50 employees, out of the 3,500 employees anticipated at the height of the construction. IFC reported that CSAIL was in the process of developing a Human Resources (HR) policy and procedures to meet relevant Performance Standards and Pakistani national requirements.²³ KPCL was expected to also use CSAIL's HR policy and procedures. In the interim, IFC reported that CSAIL was applying its Hong Kong based parent company's HR Policy to KPCL's small Chinese and Pakistani workforce.

IFC noted that CSAIL's HR Policy would include commitments to provide workers with documented information regarding their rights, freedom of association (FoA), fair treatment of migrant workers, proper management of worker accommodation, non-discrimination and equal opportunity, management of workers employed by third parties/contractors, amongst other things. IFC noted that the project's Environmental and Social Management System (ESMS) would identify and ensure compliance with laws and regulations of host country applicable to its operations. As part of the project's ESMS, IFC required the Company to ensure that the EPC contractors would develop a detailed construction E&S management plan prior to initiation of major construction.

IFC noted that Pakistani national labor law recognizes workers unions, and that the project would not restrict employees' freedom of association.

In relation to managing contractors, IFC noted that the Karot project was required to develop a contractor labor management plan to ensure contractor practices complied with GoP law and IFC

²⁰ IFC 2012 Sustainability Policy, para. 28. See also ESRP3, para. 2.1.

²¹ *Ibid.*

²² IFC 2012 Sustainability Policy, para. 7, 9 and 22.

²³ IFC E&S Review Summary, project number 36008, available at <https://bit.ly/3rkE4Sq> and as documented in the ESAP for IFC's equity investment in CSAIL (project number 34062).

requirements. The project's HR policy was expected to include a worker/contractor grievance mechanism that would facilitate the raising of grievances from workers to the relevant line managers for mutually acceptable resolution. Where there was conflict between local custom and national labor regulations preventing satisfactory resolution of worker grievances, KPCL would convene a body made up of local leaders, government authorities and contractor representatives to address this conflict.²⁴ Further, as agreed in the ESAP, KPCL, EPC contractors and subcontractors would be required to incorporate a provision for appropriate dispute resolution to address potential conflict between national labor regulations and local customary practice in all labor contracts.²⁵

In relation to Occupational Health and Safety (OHS), IFC's ESAP required the project to implement a comprehensive OHS plan applicable to all site workers. However, at the time of IFC's pre-investment due diligence, KPCL had yet to hire any OHS managers to oversee the safety performance of the EPC contractors and subcontractors.²⁶

IFC's investment disclosures indicated that the company would engage a government-certified, armed private security company and implement standard site security arrangements such as fencing, controlled access and checkpoints. It further noted that armed government security may also maintain security of the project area as a whole. As proposed to be implemented in the project's management plan, IFC concluded that these arrangements would be in line with requirements of PS4. However, prior to legal commitment, the documentation reviewed by CAO to date does not include any specific assessment of whether the project applied relevant PS4 security requirements on the training and conduct of private security personnel and conveyed the same principles to government security personnel.

While the disclosed ESAP provided for implementation of all measures by December 2015, IFC and the Company agreed that some measures related to the contractor's construction E&S management plan, appointment of E&S Advisors and inclusion of dispute resolution provision in contractor and sub-contractor labor contracts had implementation schedule to August 2016.²⁷

Construction of the Karot project commenced in January 2016.²⁸ IFC conducted a site visit to the project in April 2016. IFC noted that the management plans with the Contractor were fit for purpose and only a few remained to be reviewed by IFC. While IFC noted progress in the preparation of various E&S management plans, apparently serious OHS implementation issues were reported. These included (i) insufficient communication of OHS requirements from project management to project level staff; (ii) a lack of relevant supervisory staff; (iii) inconsistent use of worker personal protective equipment. IFC was also concerned that the majority of the 800 workers who were undertaking construction activities at the time of IFC's visit had not been provided with OHS or other job-related training. IFC noted that the Company would follow up immediately on identified OHS gaps, though it is not clear if a specific action plan was agreed.

IFC's Board approved its investment in the Karot project in May 2016. At the time of investment approval, IFC noted that the project had completed key requirements of the ESAP including (i) appointment of qualified staff, (ii) development of detailed E&S management plans, and (iii) appointment of E&S Advisors. However, one month prior to presenting the investment to Board for approval, IFC's site visit documented potential serious OHS implementation gaps. These gaps were not clearly presented in investment approval documentation. Accordingly, the basis on which

²⁴ IFC E&S Review Summary, project number 36008, available at <https://bit.ly/3rkE4Sq>.

²⁵ IFC E&S Review Summary, ESAP, project number 36008, available at: <https://bit.ly/3rkE4Sq>.

²⁶ IFC E&S Review Summary, project number 36008, available at <https://bit.ly/3rkE4Sq>.

²⁷ IFC E&S Review Summary, ESAP, project number 36008, available at: <https://bit.ly/3rkE4Sq>.

²⁸ The Diplomat, January 13, 2016, China Powers up Pakistan: The Energy Component of the CPEC available at <https://bit.ly/3liLd3Z>.

IFC reached the conclusion that the client was on track with its E&S commitments at the time of investment approval is not well documented in the materials reviewed by CAO to date.

In November 2016, IFC legally committed to the investment.

Pre-investment E&S Due Diligence: Preliminary Conclusions

Based on a preliminary review of IFC's preparation of the Karot project as outlined above, CAO has questions as to whether IFC's E&S due diligence met the standard of being commensurate to risk. Labor related risk factors on the project included the remote location, the large projected construction workforce, the need for significant amounts of workforce housing, and the need for armed security. In this context, potential concerns regarding IFC's pre-investment E&S due diligence for the project include: (a) the level of IFC's review of the project's labor related assessments and management plans prior to the commencement of construction, (b) the level of IFC's review of the maturity and effectiveness of the clients' E&S management systems (including the track record of the client and the EPC contractors in relation to labor issues), and (c) the extent to which IFC assured itself that known shortcomings in the project's management of workplace safety risks were being addressed prior to IFC making its investment.

3.3 IFC Supervision

This section summarizes IFC's E&S supervision requirements and IFC supervision of the Karot project up to April 2021, and CAO's initial review of IFC's performance in relation to the issues raised in complaints.

IFC Supervision Requirements

IFC's investment supervision commences from legal commitment until the investment is closed. During this period, IFC is required to supervise the client's compliance with the Performance Standards and other specific E&S requirements, including agreed ESAP items.²⁹ As set out in IFC's Environmental and Social Review Procedures (ESRP), "the purpose of supervision is to obtain information to assess the status of project's compliance with the Performance Standards 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."³⁰

If a client fails to comply with its E&S commitments, IFC will "work with the client to bring it back to compliance, and if the client fails to reestablish compliance, IFC will exercise its rights and remedies, as appropriate."³¹

IFC Project Supervision

IFC's supervision of the project commenced following IFC's legal commitment to the investment in November 2016. IFC made its first disbursement for the project in April 2017. Between September 2017 and July 2020, IFC made a further nine disbursements to the project. Between January 2017 and December 2019 IFC conducted multiple site visits. Due to the Covid-19 pandemic, IFC conducted three virtual supervision visits between April 2020 and January 2021.

²⁹ IFC 2012 Sustainability Policy, para. 45.

³⁰ The ESRPs are IFC staff level actions ESRP 6.1, April 2013 - <https://bit.ly/2XntNa5>.

³¹ IFC 2012 Sustainability Policy, para. 24.

As part of its supervision structure for this project, IFC and project financiers engaged an independent Lenders' E&S Consultant to perform E&S monitoring.³² IFC typically coordinated site supervision visits with the Lenders' E&S Consultant and, held meetings with management of both KPCL and the EPC. IFC noted that these supervision visits included meetings with randomly selected groups of workers.

Regarding HR policies and procedures, IFC informed CAO that KPCL and the EPC developed HR policies and procedures prior to the commencement of construction. IFC reported that the KPCL HR policy included relevant annexes relating to hiring and termination requirements. In relation to workers' accommodation, IFC advised that KPCL and the EPC contractors had developed an accommodation plan consistent with the joint IFC/EBRD guidance note "*Workers' Accommodation: Processes and Standards.*"

There were two worker fatalities at the project site in 2017 and IFC's supervision documentation notes OHS performance and contractor performance as high-risk. In response to these incidents and in advance of an IFC disbursement in May 2018, IFC required the Company to prepare root cause analysis reports and complete a safety requirement report of its site. The root cause analysis reports were reviewed and cleared by an OHS consultant prior to IFC's disbursement.

Following a site visit in April 2018, IFC noted that the project had established an ESMS which had incorporated all construction ESMPs. IFC noted that a corrective action plan had been developed to address gaps in relation to site safety and workers' use of personal protective equipment (PPE). Following a subsequent visit in November 2018, IFC recorded some improvements in the use of PPE. IFC also noted the need for a food subsidy to be provided by the EPC and all subcontractors to their workers in order to meet the IFC guidance on provision of services to workers who live in company provided accommodation at the project site.³³

In early 2019, IFC received anonymous emails from KPCL workers and an email from the Pakistan Federation of Building and Wood Workers (PFBWW) raising concerns on a range of labor issues including discrimination against Pakistani workers, lack of a functional grievance redress mechanism and allegations that workers who raised complaints had been terminated by way of retaliation. PFBWW requested IFC to facilitate discussions with KPCL management to negotiate workers' demands through a formally registered labor union. Subsequent IFC supervision of the project shows an enhanced focus on labor and working conditions. IFC met with the project's workers council, an advisory group made up of workers nominated by project management. IFC noted that KPCL and its EPC team held meetings with PFBWW. IFC's view at this time was that KPCL was in general in compliance with IFC PS2 and Pakistani law with possible exceptions related to social security pension contributions, annual salary increases and provision of food to workers accommodated on site. IFC requested the project engage a Pakistan labor lawyer to review and certify the project's employment contract templates.

IFC's December 2019 supervision visit report noted that an IFC labor consultant had recently completed a labor assessment for the project. The labor assessment reviewed the project's compliance with PS2 requirements. The labor consultant concluded that the project had worked actively to develop appropriate management systems to improve compliance on labor and working conditions but noted gaps in implementation. Key labor issues identified were: (i)

³² Mott McDonald, March 30 2017, Karot hydropower project achieves financial close, Pakistan. Available at <https://bit.ly/3CmYIM4>.

³³ IFC/EBRD Guidance on Workers' Accommodation (2009) stipulates that "Charging fees for the accommodation or the services provided to workers such as food or transport should be avoided where workers do not have the choice to live or eat anywhere else, or if deemed unavoidable, should take into account the specific nature of workers' accommodation. Any charges should be transparent, discussed during recruitment and specified in workers' contracts. Any such charges should still leave workers with sufficient income and should never lead to a worker becoming indebted to an employer", (page 19) available at <https://bit.ly/3dS8cih>.

deductions from workers' salaries for personal protective equipment; (ii) poor quality of workers' accommodation; (iii) improper overtime utilization and allocation of leave allowance; (iv) lack of a workers' organization on site (although there was no indication that the project had prevented workers from joining a union); (v) less favorable treatment of Pakistani workers vis-à-vis Chinese workers undertaking similar work; and (vi) lack of awareness of the project's grievance redress mechanism among Pakistani workers. To address these gaps moving forward, a timebound remedial action plan was developed.

In February and March 2021, IFC consultants completed separate labor and freedom of association assessments. These assessments documented improvements in relation to some of the grievances raised by workers, in particular the construction of additional accommodation for workers and improved access to water. However, the assessments also identified ongoing concerns regarding poor living conditions in worker accommodations, company practices in response to COVID-19, poor workplace safety practices, discrimination between Chinese and Pakistani workers, and limitations on freedom of association. Recommendations were provided to IFC to ensure appropriate corresponding corrective actions were requested of the client. IFC's supervision documentation in 2021 also noted material risks associated with the project's security arrangements. Consequently, IFC recommended that KPCL update their Security Management Plan and including a need to engage with the government security forces in relation to the project's commitment to international standards regarding the use of force and protection of human rights.

Project Supervision: Preliminary Conclusions

During investment supervision, IFC was aware of a range of concerns related to labor and working conditions, and occupational health and safety at the project site. In response to complaints which IFC received starting in 2018, IFC enhanced its supervision of labor related issues at the project, including by commissioning third party specialized labor assessments. This resulted in some improvements, for example in relation to the provision of additional accommodation being constructed on site and access to water. However, IFC's supervision documentation also records ongoing concerns regarding poor living conditions in worker accommodations, poor workplace safety practices, discrimination between Chinese and Pakistani workers, and limitations on freedom of association. IFC has taken steps to address concerns related to OHS, working conditions, and worker accommodation, by corrective action plans as conditions of subsequent financial disbursements. Nevertheless, IFC supervision documentation indicates that these issues have persisted through the life of IFC's investment. In this context, and considering that construction of the project has been ongoing for more than six years, CAO has questions as to whether IFC's supervision has been sufficient to identify and address E&S compliance issues as required by the Sustainability Policy.

4. CAO Decision

The Karot-02 and 03 complaints raised concerns regarding a range of PS2 issues including: working conditions and terms of employment (para.10); workers' accommodation (para. 12); workers' collective bargaining through a workers' union (para. 13 and 14); discrimination and fair treatment (para. 15); retrenchment (para. 18); grievance mechanism (para. 20), and safe work environment (para. 23). The complainants also allege that the presence of security personnel (PS4 para 12) is a concern since it creates an intimidating atmosphere that impacts the workers' ability to freely exercise their rights in the collective bargaining process. The Karot-02 complaint from a former worker also raises concerns which are individual to that person (unfair dismissal and withheld wages upon job termination).

Under the 2013 Operational Guidelines, the purpose of a CAO compliance appraisal is to ensure that compliance investigations are initiated 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 takes into account the following criteria in determining whether it is appropriate to initiate a compliance investigation in response to a complaint:

- Whether there is evidence of potentially significant adverse environmental and/or social outcome(s) now, or in the future
- Whether there are indications that a policy or other appraisal criteria may not have been adhered to or properly applied by IFC/MIGA
- Whether 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 this case CAO has made a decision to investigate based on criteria 1 and 2.

Evidence of potentially significant adverse environmental and/or social outcome(s) now, or in the future

IFC project documentation identified substandard living conditions in worker accommodations, poor workplace safety practices, discrimination between Chinese and Pakistani workers, and limitations on freedom of association that are consistent with those raised by the complainants. While these issues were picked up through IFC supervision, it is not clear that they were resolved in compliance with IFC standards during the 6-year construction period of the project. In the context of a large construction project with significant E&S risks and impacts, CAO's preliminary review of IFC supervision documentation and other available evidence indicates potentially significant adverse impacts on workers, specifically in relation to worker health and safety as well as workers' ability to organize.

Indications that a policy or other appraisal criteria may not have been adhered to or properly applied by IFC/MIGA

CAO acknowledges that the IFC has taken measures to improve the client's labor management performance. Nevertheless, CAO's preliminary review has found indications that IFC may not have complied with its policy requirements related to the issues raised in the complaints. These include:

- i. There is a lack of documented analysis of the client's labor related management plans during IFC's pre-investment review of the project.
- ii. There is a lack of documented assessment of client and contractor capacity to manage complex labor and OHS aspects of the project to IFC standards prior to investment.
- iii. There is a lack of clarity as to how IFC addressed serious on-site OHS concerns that were identified during a pre-investment site visit.
- iv. Labor and OHS compliance issues identified by IFC and external consultants have persisted throughout the construction period of the project.

In this context, CAO has decided to conduct a compliance investigation into the following labor issues raised by the Karot-02 and 03 complaints: (a) discrimination in the provision of worker services; (b) freedom of association; (c) workplace health and safety; (d) wage and retrenchment practice; (e) worker grievance handling; and (f) project security arrangements. In addition to addressing the specific concerns regarding adverse impacts raised by the Karot construction workers, CAO finds value in a compliance investigation in this case, given IFC's ongoing equity exposure to the parent company. This provides an opportunity for lessons from Karot to be integrated into IFC's supervision of any future CSAIL construction projects.

CAO has, however, decided not to conduct a compliance investigation in relation to the individual (unfair dismissal and payment) concerns raised in the Karot-02 complaint. As noted in previous CAO compliance appraisals, disputes between an employer and an individual employee that relate to working conditions or terms of employment do not usually raise substantial concerns regarding the E&S outcomes of a project which necessitate a CAO investigation.³⁴ Further, as the complainant has ceased communication with CAO, CAO is not in a position to understand whether the individual issues raised in the Karot-02 complaint present potentially significant adverse outcomes.

CAO will proceed with an investigation in accordance with the CAO Policy. The Terms of Reference for this investigation are presented in Annex C.

³⁴ See CAO compliance appraisal report of IFC investment in Bank Alfalah, November 2015, available at: <https://bit.ly/3E7zTz8>. CAO compliance appraisal report of IFC investment in Harmon Hall, April 2015, available at <https://bit.ly/3l3tgQK>.

Annex A: Perspective of Karot-02 complainant and Company on raised concerns (from CAO Assessment Report)

	Complainant	KPCL
Drinking Water	<p>The complainant raised concerns about stark differences in the <i>working and living conditions</i> of Pakistani workers as opposed to Chinese workers.</p> <p>It is alleged that, as opposed to their Chinese counterparts, the Pakistanis are treated poorly, lodged in <i>substandard facilities, not provided with potable water, and have no access to transportation services</i> to commute around the worksite.</p>	<p>Potable water is provided at easily accessible areas around the project site, offices, and in living areas. Further, KPCL maintains that to ensure quality, the supplied drinking water is tested internally twice a month and once a month by an external third party. It is noted that the external quality control procedure was suspended due to COVID restrictions though the company noted it would resume in September 2020. However, internal testing of water quality is still ongoing, and according to IFC, Mott Macdonald (a third-party consultant hired as technical and E&S advisor by the project financiers) has always indicated compliance with the National Standards for Drinking Water Quality (NSDWQ).</p>
Accommodation Facilities		<p>There are recognized concerns about one of the accommodation facilities. To address these, KPCL plans to build additional rooms. CAO was informed that,</p> <ul style="list-style-type: none"> • At the Azad Pattan site, 29 new rooms were constructed in 2019 and construction of additional 120 rooms was underway. • In 2020, 14 new rooms were constructed at the Karot site Section 3 and 146 new rooms are under construction in Section 1 area. <p>KPCL contends that the workers' accommodation is adequate and well organized. They further highlighted certain improvements that were made such as providing one electric fan for every two workers, and new geysers in washrooms to supply hot water, amongst others. It is also noted that the company provides Rs. 3,000/- per month for food charges and free laundry service to all Karot project workers and that they have also installed automatic washing machines in sufficient numbers in workers' accommodation facilities.</p>
Transportation for Workers		<p>Transportation services is currently provided for 4000 workers including both Pakistani and Chinese workers. It is also noted that efforts are being made to add more vehicles.</p>
Employment Terms	<p>The complainant noted that upon termination of his employment from work he was not paid wages he believed he was entitled to according to his contract.</p> <p>The complainant also alleged widespread concerns about other Pakistani workers' employment terms. It is claimed that these workers are hired without contracts, not paid adequate salaries for their qualifications, and are unfairly terminated. As with the complainant who filed the complaint, CAO was informed that the other affected workers also preferred to stay anonymous due to fear of losing their jobs.</p>	<p>KPCL maintained that all Karot project workers have been issued a uniform certified "Employment Contract" which was also approved by IFC.</p> <ul style="list-style-type: none"> • The human resources department issues salary slips all Karot project workers and payment of minimum wages and overtime complies with Pakistani labor laws. • Upon separation with workers, pending payments are disbursed through full and final settlement including service gratuity, which is calculated according to national labor laws.

Grievance Mechanism		<p>There is a Grievance Redressal Mechanism (GRM) in place through company complaint boxes and with a complaint lodging procedure instituted. Under the GRM are Grievance Redressal Committees that meet monthly to handle received complaints. Further, KPCL reported to have established a Workers' Council and Management Committee (WCMC) in accordance with Pakistani labor laws. The company also stated that WCMC meets regularly and they provide a bridge between the management and employees for smooth resolution of conflicts.</p>
----------------------------	--	---

Annex B: Perspective of Karot-03 complainants and Company on raised concerns (from CAO Assessment Report)

	Complainants	KPCL
Workers' Organizations	<p>It is alleged that, contrary to PS2 requirements, Pakistani national law and international law, KPCL has restricted the workers' right to freedom of association thus hampering their ability to collectively bargain with the company. Specifically, KPCL is noted to have interfered with the Awami Labor Union (ALU) registration process thus delaying the ability of the union to operate. At the same time, the complainants allege that a company-controlled union ("yellow" union) – Social Hydro 16 Union (SHLU) - was speedily registered such that none of the ALU's workers or office holders at the Karot project site were aware of its existence.</p> <p>The complainants also claim that fines are being imposed on workers without proper investigation while some are being fired without justification and compensation.</p> <p>According to the complainants, workers are watched and are not allowed to gather, meet, and discuss among themselves, and union office bearers have been repeatedly threatened and falsely accused by KPCL. This, coupled with the military presence at the site (see below), reflects, in the view of the complainants, anti-union behavior.</p>	<p>KPCL maintains that workers are free to unionize and that they respect workers' rights as stipulated under the Punjab Industrial Relations Act, 2010 (PIRA) and PS2. The company also noted having held several meetings with the complainants between March to September 2019. They further refuted the claims regarding having control over and/or influencing the process of union registration. KPCL argues that: i) they were not privy to workers joining ALU, ii) workers are not sacked without reason and relevant exit formalities and documentation are completed when a worker is terminated, and iii) due compensation are paid to the workers who leave the company and no fines are imposed on workers, except in case of violation of health and safety Standard Operating Procedures (SOPs), which are clearly communicated to workers for their own safety. KPCL added that the Health Safety and Environment (HSE) staff maintains related records and evidence of violations.</p> <p>Regarding SHLU, KPCL noted that not acknowledging the legally registered union and portraying it as a "yellow" union is unfortunate, and this reflects lack of confidence by the workers in this union. In relation to union registration, they claimed the registrar had turned down the registration application on legal grounds related to jurisdiction and that the court procedures took additional time to complete the registration process. KPCL maintains they are not connected to the registration process for ALU and have not created any hurdles in the process.</p>
Security Protocols and Personnel	<p>The complainants noted that the company's requirement for trade union leaders to provide 48 hours prior notice for authorized access to the premises severely restricts ALU's ability to carry out its duties.</p> <p>It is also alleged that the presence of military forces at the project site creates an intimidating atmosphere that impacts the workers' ability to freely exercise their rights in the collective bargaining process.</p>	<p>Concerning access to the project site, the company reported that the Government of Pakistan (GoP) oversees access to site and has deployed the Pakistani army for security as the project is of national importance. Consequently, the company noted that protocols and procedures for entry to and exit from the project site are prepared by the Pakistani army and have to be followed, leaving the company and its contractors with no control over such security protocols and procedures. KPCL maintains that this was conveyed clearly to the union leaders and that they had agreed to follow the procedures.</p>

<p>Workers' Health and Safety</p>	<p>The issues raised relate to KPCL not providing adequate personal protective equipment (PPE) for the workers thus posing a risk to their health and safety. In addition, it is alleged that the company has not established appropriate safety measures in response to COVID-19, for example – testing facilities, access to qualified doctors, and safety supplies have not been provided. It is also claimed that social-distancing protocols are not in place and workers are prevented from leaving the project site even in the event of the death of relatives.</p>	<p>KPCL maintains that, in addition to health and safety training given to workers, they and their contractors also provide adequate facilities and protection equipment for the workers. They also indicated that the workers' employment contract acknowledges the employer's responsibility in relation to the health and safety of the workers and working conditions at the workplace.</p> <p>To manage the COVID-19 situation, KPCL noted to have put the following measures in place:</p> <ul style="list-style-type: none"> • A detailed mitigation plan to curb the spread of the virus at the project site. This involves mandatory social distancing, use of masks and disinfectant spray, daily temperature checks and very limited movement, testing at the company's expense, and establishment of a quarantine facility for the workers. • five members of a medical team from China was deployed to the project site for additional support for the project's medical team. • five COVID-19 PCR testing machines and various medications, such as Lianhua Qingwen capsules and antibiotics, have been provided at the site facilities, where the medical team provides periodic testing and treatment. • A telemedicine system to provide further assistance with health care consultancy, COVID-19 prevention guidance, and other emergency guidance and services.
<p>Terms of Employment and Retrenchment</p>	<p>The complainants argue that the KPCL workers' wages are inadequate when compared with workers in the same line of work in Pakistan. It is claimed that KPCL workers do not receive the benefits provided by Pakistan's national law, including increments, gratuity, and leave. Additionally, they raised concern that there were no difference in salaries paid to skilled and unskilled workers.</p> <p>The Complainants further alleged that the terminations of workers carried out by the company without justification or compensation violate the IFC policy on retrenchment.</p>	<p>KPCL reiterated that their human resources policies have been developed in line with PS2 requirements and Pakistani labor laws. These policies are noted to have been adopted by all their contractors too. They further indicated that the certified "Employment Contract" issued to all workers at the project site was prepared by KPCL's legal firm and reviewed by IFC and FTA (Finance Technical Advisor).</p> <p>Regarding remuneration, KPCL noted that overtime is paid in accordance with applicable labor laws. They also noted that salary increment is not legally required and is at the employer's discretion to award it based on performance. KPCL also informed CAO that all the currently active workers have been registered with the Employees Old-Age Benefits Institution (EOBI) and Punjab Employees Social Security Institution (PESSI), and their contributions are being paid on a regular basis.</p>
<p>Grievance Mechanism</p>	<p>It is alleged that despite several requests by the complainants for the company to establish a grievance redress mechanism (GRM), KPCL is yet to have one in place.</p>	<p>KPCL noted that, in line with PIRA and PS2 requirements, a GRM and the WCMC were established to address workers' grievances. CAO was informed that WCMC meets every two months, although these meetings could not be</p>

	<p>The lack of a GRM hinders the workers' ability to raise concerns with KPCL.</p>	<p>held as frequently due to COVID restrictions. Nonetheless, KPCL indicated that workers could access the complaint boxes which are available in all labor camps, or lodge complaints directly with HR and HSE personnel via phone calls.</p> <p>According to KPCL, WCMC comprises of 20 worker representatives nominated by the workers from different sub-contractors, and 12 members from management. The WCMC provides a bridge between the management and employees for smooth resolution of conflicts and engages the workers in its routine activities without any disturbance. The Company indicated that, since the establishment of the WCMC, a number of worker grievances have been resolved, including issues related to control of food prices, increasing the drinking water cooler ratio in camps, the immediate leave approval process, timely payment of wages, and establishment of a dispensary under the PESSI.</p> <p>KPCL explained that WCMC follows a complaint-lodging procedure that includes ability to file anonymous complaints. They further noted that the GRM procedure is shared with all workers through daily "Toolbox Talks".</p>
--	--	---

Annex C: Terms of Reference for Karot 02-03 Investigation



January 21, 2022
Office of the Compliance Advisor Ombudsman (CAO)

Terms of Reference for Compliance Investigation of IFC

*IFC Investment in Karot Hydro
(IFC Project #36008 and #34062)
Pakistan*

About CAO

The Office of the Compliance Advisor Ombudsman (CAO) is an independent recourse and accountability mechanism that receives complaints from communities and persons who may be affected by the projects that the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA) support. The 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](#)”).

Through the exercise of its complementary 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/MIGA and reduce the risk of harm to people and the environment.

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

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."*³⁵ 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.³⁶

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

In November 2014, IFC committed to a 15 percent equity investment for US\$125 million in China Three Gorges South Asia Investment Limited (CSAIL). CSAIL was established to make renewable power generation projects in Pakistan. In May 2016, IFC approved a US\$100 million loan to finance the construction, operation, and maintenance of a 720MW run-of-the-river hydropower plant on the Jhelum River, by Karot Power Company Limited ("KPCL", or "the Company") a special purpose vehicle and majority owned by CSAIL. The 720MW run-of-the-river hydropower is the Karot project. Accordingly, IFC is exposed to the Karot project via its loan to KPCL and its equity in CSAIL.

The total cost for the Karot project is estimated at US\$1.74 billion. The construction of the Karot project commenced in 2016 and it is expected to complete by April 2022. IFC's categorized the environmental and social (E&S) risk of the Karot project as Category A.

The Complaints

Karot-02 complaint was filed by a former worker at the project who raises both individual concerns and concerns which prefacia are systemic in nature. The Karot-02 individual concerns are that he was unfairly dismissal and his wages were withheld upon job termination. His allegations of a

³⁵ CAO Policy, Sec. X, para. 76.

³⁶ CAO Policy, Sec. X, para. 77.

systemic nature are that the project discriminates against local Pakistani workers as compared to Chinese workers in relation to the provision of worker services, including access to drinking water, conditions of accommodation, and access to transportation at the project site. As detailed in CAO's compliance appraisal report, CAO decided not to proceed with an investigation in relation to the Karot-02 individual concerns.

The Karot-03 complaint was filed with CAO in July 2020 by representatives of Building and Wood Workers International (BWI) and the Pakistan Federation of Building and Wood Workers (PFBWW). The complaint was submitted on behalf of the Awami Labor Union at the KPCL. The complaint raises concerns about adverse project impacts on approximately 3,000 Pakistani workers at Karot. The complainant raises concerns regarding Company interference in union activities; (ii) Occupational Health and Safety (OHS), including Covid-19 procedures; (iii) employee wage levels and retrenchment; (iv) the Company's grievance mechanism; and (v) the presence of security personnel creating an intimidating atmosphere that impacts workers' ability to participate in union activities.

Decision to Investigate

On January 21, 2022, CAO Director General decided to trigger an investigation of IFC's E&S performance in relation to IFC investments and financial exposure to the Karot Power Company Limited.

CAO decided to conduct a compliance investigation into the following labor issues raised by the Karot-02 and 03 complaints: (a) discrimination in the provision of worker services; (b) freedom of association; (c) workplace health and safety; (d) wage and retrenchment practice; (e) worker grievance handling; and (f) project security arrangements.

The terms of reference for the CAO's investigation of the Karot project were prepared in accordance with CAO Policy paragraphs 96 and 118.

Investigation Terms of Reference

Where, as in the present case, the CAO appraisal process results in a decision to investigate, CAO develops 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; and*
- 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.³⁷*

³⁷ CAO Policy, Sec. X, para. 118.

A. Objective, scope, and methodological approach

Objective and scope: As established by the CAO Appraisal Report, CAO will conduct a compliance investigation of IFC's investments in Karot project in relation to the systemic issues raised in the Karot-02 complaint and issues raised in the Karot-03 complaint.

In relation to these matters, 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; and
 - 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.³⁸

The investigation will focus on IFC's appraisal and supervision of its investments that provide exposure to the Karot project with respect to their systems and their application to prevent and respond to labor and security concerns.

The investigation will examine whether IFC adequately appraised, structured and supervised its investments that provide it exposure to the Karot project. It will also consider whether IFC ascertained sufficient evidence of the Karot project's compliance with relevant PS2 and PS4 requirements. If project level gaps were or should have been identified, the investigation will consider whether IFC took appropriate action. The investigation will determine whether IFC/MIGA has complied with its E&S Policies and whether there is Harm related to any IFC/MIGA non-compliance.

In making findings regarding Harm and whether any Harm is related to IFC/MIGA non-compliance with its E&S Policies, CAO may consider the client's environmental and social performance.

Methodological Approach: CAO will base the compliance investigation on information available to CAO from interviews, statements, reports, correspondence, CAO observations of activities and conditions, and other sources that CAO deems relevant.³⁹

The compliance investigation process and associated 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 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.*⁴⁰

³⁸ CAO Policy, Sec. X, paras. 112 - 114.

³⁹ CAO Policy, Sec. X, paras. 115 and 117.

⁴⁰ CAO Policy, Sec. X, para. 120.

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.⁴¹

B. Limitations of the investigation

CAO typically conducts a site visit to the project as part of its compliance investigation. This investigation has been initiated during the Coronavirus-19 pandemic. At the time writing, the World Bank Group has implemented restrictions on staff travel. These restrictions may limit process by which CAO conducts this investigation.

C. External expert

CAO will engage one or more external labor experts to assist in the investigation. For this compliance investigation, CAO considers the following qualifications as necessary:

- Significant expertise and experience in labor issues and international good practice regarding unions, grievance mechanisms and use of security forces.
- Significant expertise in conducting reviews of institutional approaches to labor issues, including policies, procedures, implementation, and incident response.
- Significant expertise in the application of Performance Standard 2 to large infrastructure projects.
- Knowledge of Pakistan labor law.
- Demonstrated ability to analyze policies and practices and develop proposals for reform in complex institutional contexts.

D. Compliance investigation schedule, timeframe, and reporting requirements

Under CAO Policy Section X at paragraph 121, a draft compliance investigation report should be circulated within one year of an appraisal report's disclosure. By February 2023, a draft Compliance Investigation Report for this case will be circulated to IFC/MIGA Senior 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.

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 MAPs.

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 IFC/MIGA 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

⁴¹ CAO Policy, Sec. X, paras. 116 - 117.

IFC/MIGA Senior Management and circulated to the Board, CAO will notify the public on its website of the investigation's completion.

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.

CAO will submit comments on the proposed MAP to the Board, and the Complainants may submit to CAO a statement on the proposed MAP and the adequacy of consultations for circulation to the Board. Upon the Board's approval of the MAP, the compliance investigation report, management report, and MAP will be published on CAO's website.⁴²

⁴² CAO Policy, Sec. X, para. 138.