



June 1, 2015
Office of the Compliance Advisor Ombudsman (CAO)

COMPLIANCE APPRAISAL: SUMMARY OF RESULTS

*IFC Advisory Services Project with Vizhinjam International Seaport Limited, India
Project #28991*

Complaints 01 to 03

Executive Summary

In 2009, IFC initiated an Advisory Services (AS) project to support the Government of Kerala (GoK), India, in designing and implementing a bidding process for the development of an international port (“the port”). The GoK acted through a wholly owned company, Vizhinjam International Seaport Limited (“VISL” or “the client”).

The objective of the AS project was to assist the client in structuring and implementing a competitive process to select a company to construct, operate, and manage the port. The AS project extended to the preparation of environmental and social impact assessment documentation required for the project to receive clearance from the Indian Ministry of Environment and Forests (MoEF). IFC’s role also included marketing the project to potential bidders in India and internationally.

In March 2013, IFC concluded its role in the AS project. At this point, the port development had been put to tender but GoK had decided not to award the contract. Subsequently, however, GoK reopened bidding for the port development and in May 2015 a GoK committee recommended the award of the port project to the sole bidder, Adani Ports and Special Economic Zone Ltd (APSEZ).

In 2012 and 2013, CAO received three complaints regarding the project from potentially affected communities. Due to the related nature of the issues raised, all three complaints are considered in this compliance appraisal.

The first complaint, dated August 2012, was filed by a representative of the Kerala Hotels and Restaurants Association, a former representative of the State Fisheries Department and a social activist. The second complaint, dated September 2012, was filed by a local fishing group, the “Kerala Swathantra Malsya Thozhilali Federation” (Kerala Independent Fish Workers Federation). The third complaint, dated April 2013, was filed by 14 residents of Mullor village, located near the project site.

The purpose of a CAO compliance appraisal is to determine whether an investigation of IFC’s environmental and social (E&S) performance is required in relation to a project. In deciding whether to initiate an investigation, CAO weighs factors including the magnitude of the E&S concerns raised by a complaint, results of a preliminary review of IFC’s E&S performance in relation to these issues, and a more general assessment of whether the complaint raises issues of systemic concern for IFC.

As such, this appraisal considers whether IFC acted in accordance with relevant policy requirements in its review and execution of the AS project. More specifically, this appraisal considers whether, in relation to the concerns raised by the complainants, IFC provided advice that was consistent with its Performance Standards. It also considers the adequacy of IFC’s E&S policy framework in the context of this AS project.

On the basis of available information, CAO considers that the complaints raise potentially significant concerns about the E&S impacts of this project. The complaints also raise questions about the application of IFC's E&S requirements to the project. These include:

- a. whether IFC's advice in relation to E&S issues was consistent with the Performance Standards, particularly regarding the:
 - assessment of the environmental and social impacts of land-based infrastructure associated with the project;
 - application of Performance Standard 5 as it applies to economic displacement; and
 - application of Performance Standards 1 and 6 as they apply to stakeholder consultation and project impacts on ecosystem services.

- b. whether IFC's policies, procedures, and practices as they were applied to the selection and structuring of this AS project provided an adequate level of guidance and protection in the context of IFC's broader commitments to sustainable development.

On the balance of considerations, CAO has decided to conduct a compliance investigation of IFC's E&S performance in relation to this AS project. Terms of reference for this compliance investigation will be prepared in accordance to CAO's Operational Guidelines.

About CAO

CAO's mission is to serve as a fair, trusted, and effective independent recourse mechanism and to improve the environmental and social accountability of IFC and MIGA.

CAO (Office of the Compliance Advisor Ombudsman) is an independent post that reports directly to the President of the World Bank Group. CAO reviews complaints from communities affected by development projects undertaken by the two private sector arms of the World Bank Group, the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA).

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

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Acronyms

Acronym	Definition
AS	IFC Advisory Services
APSEZ	Adani Ports and Special Economic Zone
CAO	Office of the Compliance Advisor Ombudsman (IFC and MIGA)
E&S	Environmental and Social
EIA	Environmental Impact Assessment
ESIA	Environmental and Social Impact Assessment
ESRP	Environmental and Social Review Procedures
FASA	Financial Advisory Services Agreement
GIIP	Good International Industry Practice
GoK	Government of Kerala
IFC	International Finance Corporation
MoEF	Indian Ministry of Environment and Forests
PPP	Public-Private Partnership
PS	Performance Standards
TOR	Terms of Reference
VISL	Vizhinjam International Seaport Limited

I. The Compliance Appraisal Process

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

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

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

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

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

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

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

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

II. Background

IFC Advisory Services Project

In 2009, IFC initiated an Advisory Services (AS) project to support the Government of Kerala (GoK), India, in designing and implementing a bidding process for the development of a greenfield international port in Vizhinjam, Kerala (“the port”).

The port was to be developed using a Public Private Partnership (PPP) model. The GoK acted through a wholly owned company, Vizhinjam International Seaport Limited (VISL or “the client”), which was to select, through competitive bidding, a private partner to construct, finance, operate, and manage the port.

The objective of the AS project was to assist the client with structuring and implementing the bidding process. Two previous rounds of bidding, in 2004-06 and 2007-09, led by the GoK had not been successful. IFC’s AS project extended to the preparation of E&S impact assessment documentation required for the project to receive clearance from the Indian Ministry of Environment and Forests (MoEF).

The AS project was divided into two main phases:

- Phase I involved due diligence and preparation for the bidding process (due diligence included conducting a full legal, technical/environmental, and financial review).
- Phase II involved implementation, including Request for Proposal preparation, marketing, and bidding processes.

The Financial Advisory Services Agreement (FASA – dated November 2009) between IFC and the client stated that IFC would assume overall oversight of the client’s consultants and that IFC-hired consultants would direct the development of the Environmental Impact Assessment (EIA) for the port, a requirement for the project to proceed under Indian law.

In March 2013, IFC concluded its primary role in the project. IFC’s AS Project Completion Report (March 29, 2013) recorded that the GoK had decided not to award the project. Subsequently, however, GoK reopened bidding for the port development and in May 2015 a GoK committee recommended the award of the port project to the sole bidder, Adani Ports and Special Economic Zone Ltd (APSEZ).¹ At the time of writing, IFC had no ongoing involvement in the project, however, any future exposure to the construction of the port, either directly or through a financial intermediary would be of relevance in the context of CAO’s compliance mandate.

Complaints

CAO received three complaints about the Kerala Port project.

In August 2012, the first complaint was filed by representatives of affected communities, including a representative of the Kerala Hotels and Restaurants Association; a former representative of the State Fisheries Department; and a social activist. The first complaint related primarily to the design of the port project and its socio-economic and environmental impacts on tourism and fishing activities. It also raised concerns about IFC’s due diligence for the project and stakeholder consultation activities.

In November 2012, a second complaint was filed with CAO by a local fishing group, Kerala Swathantra Malsya Thozhilali Federation (Kerala Independent Fish Workers Federation). This complaint related primarily to the impact of the port on fishing activities. It also underscores concerns

¹ Business Standard (May 7, 2015) ‘Empowered Committee recommends Adani for Vizhinjam’ <http://goo.gl/gMZA4s> (Accessed May 15, 2015)

about the project's impacts on marine biodiversity, pollution, soil erosion, loss of land, and safety of the fishing community.

In April 2013, a third complaint was filed with CAO by 14 residents of the village of Mullor in the Vizhinjam area. This complaint relates to impacts on farmland and access to water in relation to infrastructure associated with the port development (in particular, road construction).

All three complaints were found eligible by CAO. As there was no agreement to participate in a dispute resolution process, all three complaints were transferred to CAO's compliance function.

III. Analysis

This section outlines the framework of IFC E&S policies and procedures as they apply to the AS project. It then analyzes IFC's approach using these standards during preparation and implementation of the project, and in the context of the issues raised by the complainants.

IFC Policies and Procedures for Advisory Services

This project was prepared and initially implemented under IFC's 2006 Policy on Social and Environmental Sustainability ("2006 Sustainability Policy") and Performance Standards (PS). The key requirement from the 2006 Sustainability Policy in relation to IFC AS projects is that "when IFC is providing advice for large scale investment projects, the Performance Standards are used as a reference in addition to national laws" (para. 30).

The Sustainability Policy and the PS were updated effective January 2012, and are now together referred to as the Sustainability Framework. The key requirement of this update in relation to AS projects is that, where E&S risks are identified, IFC will provide advice that is "consistent with the Performance Standards as a framework of good international industry practice" (para. 39). The 2012 Sustainability Policy further stipulates that when IFC provides advisory services to its clients, it strives to "achieve positive improvements in environmental and social performance, and help clients move towards greater consistency with the Performance Standards, even if they are not able to meet their full intent during the life of the advisory activity" (*Ibid.*).

IFC implements its commitments in the Sustainability Policy through its Environmental and Social Review Procedures (ESRP). These procedures outline how IFC evaluates the potential E&S risks around a proposed AS project. This project was approved under ESRP Version 4 (August 2009) and supervised under subsequent versions of the ESRP.

In accordance with ESRP Version 4 (para.11.3.3), the transaction leader for an AS project will "consider the impacts and outcomes of the AS project and determine whether the impacts and outcomes could have potential E&S risks. [...] If there are E&S risks, the Transaction Leader will include the AS Sustainability Champion and the CESI Sustainability Champion/Specialist on the AS team as peer reviewers and consult with them on how to incorporate the E&S best practices into the project".²

Neither the Sustainability Framework nor the ESRP provide specific guidance in relation to the management of E&S risks during the implementation of AS projects.

² The Transaction Leader is the IFC staff with primary responsibility for the AS project. Sustainability Champions are IFC AS technical staff trained to provide advice on E&S issues in relation to low- and medium-risk AS projects. CESI specialists are technical specialists with IFC's E&S department.

The 2006 Sustainability Policy does, however, include higher-level E&S commitments that apply to AS projects. For example, the 2006 Sustainability Policy states that efforts to “carry out its investment operations and advisory services in a manner that ‘do no harm’ to people and environment,” are “central to IFC’s development mission” (para. 8). Similar language is included in the 2012 Sustainability Policy.

Preparation of the Advisory Services Project

Review and Approval

IFC’s approval documentation for the AS project was finalized in November 2009. An experienced IFC E&S specialist was included in the team that reviewed the project. While no specific E&S analysis was prepared at this stage, IFC’s project approval documentation noted that the project was expected to have risks associated with land acquisition and potential impact on fishing communities. IFC’s approval documentation indicated that an E&S specialist would be involved in designing and overseeing the E&S aspects of the project. This was envisaged as including the engagement of consultants for the development of an environmental impact assessment (EIA) and environmental management plan (EMP), reflecting IFC’s Performance Standards. At the same time, IFC’s approval documentation noted that AS clients that are public entities were not required to adhere to IFC E&S standards.

Scope of the Advisory Service Project

The scope of the AS project was agreed between IFC, the GoK and the client in November 2009. The agreement provides that IFC would conduct due diligence and preparation for the bidding process, including conducting a full legal, technical/environmental, and financial due diligence review.

The agreement also describes consultants to be hired by the client (the “client consultants”) and by IFC (the “IFC consultants”), noting that IFC would be required to work closely with consultants retained by the client in connection with the project. IFC agreed to act as lead adviser, assuming overall oversight of the performance of client consultants including those involved with access infrastructure for the port development.

As agreed, the specific roles of the IFC consultants would include: (a) reviewing the Rapid EIA that had been prepared for the project in 2004; (b) preparing the terms of reference for an EIA for the MoEF; (c) carrying out the EIA; and (d) performing a social impact assessment for the land that would be acquired for the development.

As set out in IFC’s completion report for the project IFC’s approach to E&S issues involved : (i) the E&S risks attached to the project were identified as high; and (ii) IFC recognized prior to approving the AS project that the client did not have the capacity to undertake an EIA that was consistent with IFC’s PS. CAO also notes that the IFC completion report documented as a lesson learned from this AS project, that E&S work should be limited to scoping assessment of applicable Performance Standards with the E&S assessment itself, left for the client to conduct.

Conclusion

Based on the material reviewed in the course of this compliance appraisal, CAO finds no indication that IFC’s preparation of the Kerala Port AS project was other than consistent with its E&S policies and procedures. On the other hand, CAO has questions as to whether these requirements provided an “adequate level of protection,”³ given IFC’s higher-level E&S commitments referenced above.

³ CAO. Operational Guidelines (2013) para. 4.2.1.

IFC's key E&S policy requirement for AS projects is that its advice should be "consistent with the Performance Standards." Given that IFC recognized significant E&S risks attached to the port development CAO has questions as to whether the applicable policies and procedures provided adequate guidance on: (i) when E&S risks (including client commitment and capacity to manage such risks) should preclude IFC from engaging as an adviser to a project; and (ii) the scope of E&S responsibility that IFC should take on in relation to a high risk AS project.

Implementation of the Advisory Services Project

The issues raised by the complainants relate both to IFC's involvement in the project and to the project's potential socio-economic and environmental impacts on tourism, fishing, and farming activities. This section considers how IFC responded at each stage of the project in light of the key compliance question – whether the advisory services IFC gave its client were consistent with the Performance Standards.

Issues rated to the land-based components of the project

As noted above, IFC committed to complete the EIA and to oversee work done by client consultants related to the project. According to Performance Standard 1, the assessment of project impacts would be required to cover "associated facilities" such as infrastructure that "would not have been constructed or expanded if the project did not exist..."⁴

In January 2010, IFC's supervision documentation for the project noted that the GoK had already begun to acquire land for the project, and that this might lead to protests. In this context, IFC determined that the road and rail infrastructure associated with the port fell outside IFC's advisory mandate, but that its E&S specialists had been closely involved in the project team to provide inputs to the client on land acquisition issues. IFC stated that it also had advised the client that it should appoint a client consultant to complete an environmental and social impact assessment for connectivity infrastructure associated with the port (a Road and Rail ESIA) in addition to the ESIA for the port itself, which IFC would lead (the Port ESIA). IFC noted that the project team would continue to provide "hand holding" to the client on social impact issues, with the help of IFC E&S experts.

From this point on, issues related to land acquisition and the impacts of road and rail connectivity infrastructure were addressed by the client (albeit with some inputs from IFC) while issues related to the port itself were the direct responsibility of IFC. The client would later incorporate both the Road and Rail ESIA and the Port ESIA into a Comprehensive EIA (CEIA) that was submitted to MoEF for approval.⁵

Issues related to the project's socio-economic impacts

A Preliminary Project Plan was prepared by the IFC consultants in October 2010. The Preliminary Project Plan states that the economic viability of the project was assessed in a Cost Benefit Analysis (CBA) that included direct costs and benefits generated by the development of the port, indirect effects to the region, and costs of externalities, such as social and environmental impacts. CAO notes that the stakeholders considered for the economic evaluation did not include the local communities that would potentially be affected by the project. Also, while the plan notes that externalities should be taken into account in the overall appraisal of the project, their economic effects are not included in the CBA. Further, no indirect costs on sectors such as fishing and tourism

⁴ IFC. PS1 (2012) para. 8.

⁵ GoK. Comprehensive EIA for Vizhinjam International Seaport (Report (Final)). <http://www.vizhinjamport.in/eia-30-5-13.php> (Accessed May 15, 2015)

are accounted for in the analysis. It is thus unclear whether the CBA assigns appropriate economic value to existing industries surrounding the project location.

Issues related to the adequacy of the Port ESIA (prepared by IFC)

In April 2013, after formal closure of IFC's Advisory Services project, the IFC consultant delivered the final draft of the Port ESIA. The Port ESIA expressly excludes the infrastructural/ancillary facilities of the port, and notes that the ESIA does not analyze alternative sites.⁶

In relation to tourism, the Port ESIA sets out a prediction and assessment of socio-economic impacts including those from loss of beaches, loss to businesses, employment, and the likelihood of an increase in tourism (based on proposed cruise terminal operations at the Port). The Port ESIA also confirms that the impacts on individual resorts/hotels — where land will not be acquired but they still will be affected by the project — were not studied in detail as part of the socio-economic survey. The potential negative impacts on tourism are assessed as being of “major” significance during both the construction and operations phases. In relation to mitigation, the Port ESIA recognizes there are indirect impacts on resort owners and households having livelihoods linked to ayurvedic health resorts that would not be acquired. IFC advised these issues be assessed and mitigated under PS1 and not PS5 (Land Acquisition and Involuntary Resettlement).

In relation to fishing activities, the Port ESIA discusses the socio-economic baseline for fishing communities and recognizes that nearly 20,000 people are involved in fishing and related activities at the Vizhinjam Harbour. It recognizes both construction-phase impacts and ongoing operational-phase impacts, such as the loss of access to beaches and fishing ground, loss of income, obstructed access to the fishing harbor from south of the breakwater for fisher folk who use the harbor for catch landing, and an increased risk of accidents. The mitigation framework for socio-economic impacts on fisheries-based livelihoods points out that a robust and comprehensive Livelihood Restoration Framework should be prepared in consultation with the affected fishing community. Mitigation measures are described in terms of guiding principles that the Port developer should follow for livelihood restoration, but do not address the communities whose livelihoods are connected to the value chain for fishing (including markets, transportation, and other industry issues).

Conclusion

As to the decision to split the E&S advisory mandate, CAO considers that further analysis is required to determine whether IFC's advice on the development of a separate E&S assessment for the land-based facilities associated with the port was consistent with the requirements of PS1 (Assessment and Management of E&S Risks and Impacts), particularly in light of IFC's analysis of the client's need for extensive support in relation to E&S issues. The decision to split the E&S advisory mandate is particularly relevant to the third complaint, which raises issues related to the impacts of the port's land-based infrastructure. CAO also has questions as to whether the technical inputs that IFC gave its client about the Road and Rail ESIA were consistent with the requirements of the Performance Standards.

In relation to the assessment of the project's socio-economic impacts, CAO has questions as to the robustness of the Cost Benefit Analysis carried out by the IFC consultants, and the extent to which this analysis considers the project's impacts on the livelihoods of the communities in the immediate vicinity of the proposed port.

Finally, while a preliminary review of the Port ESIA led by IFC indicates that it was generally consistent with the PS, CAO has questions as to the following elements, which relate to the issues raised by the complainants:

⁶ Location-Specific Draft ESIA for the sea part of Vizhinjam Port, in Kerala State of India, Main Report

- whether PS5 was properly applied to the potential impacts of the project on tourism operators and fishing communities, particularly as relates to potential economic displacement; and
- whether PS1 and PS6 (Biodiversity Conservation and Sustainable Management of Living Natural Resources) were adequately considered in terms of the project's impact on ecosystem services relied upon by the local tourism and fishing industries.

IV. Decision

The decision about whether CAO should initiate a compliance investigation requires weighing a number of factors, including the likely E&S impact of a project, a preliminary review of IFC's E&S performance, and a more general assessment of whether a compliance investigation is the appropriate response to a complaint, for project-related or systemic reasons.

On the basis of available information, CAO considers that the complaints raise potentially significant concerns about the E&S impacts of the AS project. The complaints also raise questions as to the application of IFC's E&S requirements to the AS project. These include:

- a. whether IFC's advice on E&S issues was consistent with the Performance Standards, particularly with regard to:
 - assessment of the environmental and social impacts of land-based infrastructure associated with the project;
 - application of Performance Standard 5 as it applies to economic displacement; and
 - application of Performance Standards 1 and 6 as they apply to stakeholder consultation and project impacts on ecosystem services.
- b. whether IFC's policies, procedures, and practices as applied to the selection and structuring of this AS project provided an adequate level of guidance and protection in the context of IFC's broader commitments to sustainable development.

At the time of writing, CAO notes that IFC had no ongoing involvement in the project, however, any future exposure to the construction of the port, either directly or through a financial intermediary would be of relevance in the context of CAO's compliance mandate.

On the balance of considerations, CAO has decided to conduct a compliance investigation of IFC's E&S performance in relation to this AS project. Terms of reference for this compliance investigation will be prepared in accordance to CAO's Operational Guidelines.