



CAO COMPLIANCE

CAO Investigation of IFC

CAO Ref: C-I-R9-Y12-F167

August 29, 2014

CAO Investigation of IFC Investment in Minera Quellaveco SA, Peru

Office of the Compliance Advisor Ombudsman (CAO)
for the
International Finance Corporation (IFC) &
Multilateral Investment Guarantee Agency (MIGA)
Members of the World Bank Group

Executive Summary

Background

The Quellaveco mining concession is located in Peru in the Region of Moquegua. It is an undeveloped porphyry copper deposit in which Anglo American plc owns the controlling stake. In April 1993, the IFC Board approved US\$ 6 million investment to acquire a 20 percent equity investment in Quellaveco (the Company). Between 1996 and 2011 IFC participated in a number of rights issues providing US\$ 54 million in additional capital to the company to continue its development activities. In February 2012 IFC sold all of its shares in the Company to a fully-owned subsidiary of Mitsubishi Corporation. At the time of writing approval for the development of the mine was pending.

In November 2011, CAO received a complaint from *Asociación Civil Labor*, a local environmental NGO in Peru, raising concerns about the Quellaveco project's actual and anticipated impacts on local people and the environment. In response a request from CAO for documentation verifying the participation of project-affected groups, the Water Users Board of Moquegua and the *Frente Unificado de Defensa de los Intereses del Distrito de Torata* sent letters to CAO outlining their concerns in March 2012.

Based on the letters of complaint and the CAO Ombudsman Assessment Report,¹ the issues raised in the complaint can be summarized as concerns regarding:

- (a) water scarcity, the degradation of water quality, and increased competition over water resources in an arid area;
- (b) pollution, including disposal of mine tailings and consequent environmental and health risks;
- (c) land claims on the Project sites; and
- (d) adequacy of community engagement, including lack of consultation on the initial and modified Environmental Impact Assessment.

In May 2013, CAO completed a Compliance Appraisal in accordance with its Operational Guidelines. Based on the Compliance Appraisal process, CAO found that a review of certain aspects of this Project which relate to its nature as an early equity mining investment would usefully inform the application of IFC's policies and standards. CAO therefore decided to conduct a Compliance Investigation into this Project, having regard to the matters raised in the complaint, with a focus on the following questions:

- Are IFC's policies and procedures regarding environmental and social categorization of projects, as applied to its investment in Quellaveco, effective to reflect the magnitude of project risks and impacts?
- Are IFC's policies and procedures in relation to rights issues, as applied to its investment in Quellaveco, consistent with IFC's commitment to ensure that the business activities it finances are implemented in accordance with relevant environmental and social standards?
- Do IFC's policies and procedures regarding divestment from projects, as applied to its investment in Quellaveco, ensure appropriate consideration of environmental and social aspects prior to exiting?

¹ http://www.cao-ombudsman.org/cases/case_detail.aspx?id=185.

Findings

General

In reaching conclusions on IFC's E&S performance in relation to the Company, CAO recognizes that this investment was initiated at a time when IFC E&S procedures were relatively underdeveloped. CAO also recognizes that the Project was seen by IFC as having limited environmental and social risks as it was envisaged as supporting a series of feasibility studies and pilot activities ahead of the decision to proceed with the construction of a mine.

Nevertheless, CAO finds that IFC omitted to include necessary E&S requirements in the Shareholders Agreement which formed legal basis for the investment. This, CAO finds, resulted in a significant gap in terms of the Company's E&S obligations, particularly given IFC's undertaking to its Board of Directors in March 1993 that the Project would "comply with all applicable World Bank environmental and occupational health and safety guidelines."

CAO finds that the absence of E&S requirements in IFC's investment agreement made E&S supervision difficult. In making this finding, CAO acknowledges IFC's position that supervision of the Project was thorough and took account of the evolving Performance Standards. CAO also acknowledges that the subsequent development of IFC's E&S policies and procedures, means that such an oversight should not occur today.

Notwithstanding the absence of E&S requirements, CAO finds that IFC supervised the Project with reference to IFC's evolving E&S standards and policies. During supervision, IFC identified a range of social concerns regarding land acquisition and resettlement, the Project's impact on Indigenous Peoples and the adequacy of public consultation. IFC also identified potential environmental impacts, including the adequacy of the water resources needed to service the mine, and the potential for water pollution. This represented good practice.

While the Complainants' concerns had not fully been addressed at the time of IFC's divestment, CAO finds that IFC's engagement with the Company around E&S issues was generally appropriate to the stage of development of the Project. CAO notes IFC's view that the Company was broadly receptive to IFC advice on E&S issues. However, CAO also finds that key E&S issues identified by IFC in project supervision were not translated into corrective action plans. Agreeing on such plans would have been of particular relevance in relation to: (a) land acquisition activities (which IFC noted were proceeding in advance of the development of studies and plans required by IFC E&S standards); (b) the impact of land acquisition on Indigenous People, (c) issues of stakeholder engagement and (d) the more technical elements of project design and environmental impact assessment that are discussed in IFC's 2007 and 2010 supervision documentation.

CAO also finds that certain information presented by IFC to its Board in the course of this Project was incomplete. This includes statements that: (a) the Project would comply with the World Bank's environmental standards (in a context where the legal agreement did not include such requirements); and (b) exploration activities were "fully compliant with the Performance Standards," (in a context where IFC had documented gaps in compliance with the Performance Standards and was concerned about the readiness of its client to further develop the Project in accordance with these Standards).

More generally, this compliance investigation raises questions about IFC's application of the Sustainability Framework and associated procedures to the long-term E&S risk associated with early equity investments in the mining sector.

Environmental and Social Categorization

IFC categorizes its direct investments A, B or C depending on the magnitude of their E&S risks and/or impacts. Category A projects have potential **significant** adverse impacts, category B projects have **limited** potential adverse impacts, and category C projects have **minimal** or no potential impacts.

In 1993, when IFC bought its equity stake in the Company, it was acknowledged that the development of the mine would be a category A project. At the time of investment, IFC believed that the likelihood of the Project leading to a commercial development was 'high' with the expectation that the construction of a mine could begin as soon as 1997. However, the Project was categorized as B on the basis that it was focused on feasibility and pilot activities.

It is clear that there are challenges involved in categorizing E&S risks and impacts around early equity mining investments. On one hand, if feasibility work ultimately does not result in a decision to develop a mine, a project's potential E&S risks and impacts will be limited to the consequences of undertaking pre-construction activities. On the other hand, if a decision to proceed with development of a mine, particularly one in a socially or environmentally sensitive area, is made, the potential E&S risks and impacts of the project will often be significant.

CAO finds that there are good reasons for considering longer-term risks and impacts when IFC makes a decision on the E&S categorization of an early equity mining investment. First, this approach is consistent with the wording of the Sustainability Policy which requires IFC to consider "potential" (as opposed to actual, direct, or immediate) adverse E&S impacts of a project when making a decision on categorization. Second, IFC explains the rationale for its early equity business line on the basis that it is not a speculative or short term investor, but a long term partner for mining projects that have a strong possibility of being developed. This approach suggests that the prospect for development of a mine, with associated E&S risks, is significant. Finally, CAO finds that there may be advantages for IFC and its clients in terms of managing community expectations and concerns if the long term E&S risks attached to early equity mining investments are seen as being fully acknowledged rather than underplayed.

CAO finds that the concerns raised above would most effectively be addressed if IFC provided guidance that the decision as to how an early equity mining project should be categorized is to be determined on a case-by-case basis, taking into account the potential E&S impacts of the project (both immediate and long term), as well as its likelihood of development.

Applying this approach, CAO finds that IFC's Quellaveco investment would properly have been categorized A at the outset, given: (a) the magnitude of the potential impacts of the proposed mine; (b) IFC's view that it had a high likelihood of moving forward to development; and (c) the potential E&S risks and impacts of the Project in the pre-development phase, in particular potential impacts on Indigenous People.

Further, CAO finds that policy guidance is required in relation to the re-categorization of IFC projects as their risk profile develops. In reaching this finding CAO acknowledges IFC's view that the E&S categorization of committed projects is immaterial in terms of IFC's duties during project supervision. Nevertheless, CAO finds that IFC's categorization plays an important role in communicating project E&S risk to internal and external stakeholders, and as such that re-categorization in response to significant changes in the risk profile of a project may be appropriate.

Participation in rights issues

As an equity holder, IFC had the opportunity to participate in rights issues to provide the Company with capital needed to finance its ongoing project development activities. In addition to an initial investment of \$6 million in 1993, IFC contributed an additional \$54 million to the Project through rights issues between 1996 and 2011. 78.5 percent of this amount was committed after IFC adopted its E&S Performance Standards in April 2006.

CAO finds that IFC complied with existing procedures for participating in rights issues in the Company.

CAO, however, also notes that there are significant risks involved in providing additional finance to a project that has inadequate or outdated E&S obligations, or where there is evidence of non-compliance with existing E&S obligations. Given these risks, consistency with IFC's policy commitment to "ensure that the projects it finances are operated in a manner consistent with the requirements of the Performance Standards" would require IFC's participation in a rights issue to be contingent upon an appropriate review of project E&S risk. IFC's procedures as applied in the processing of rights issues for the Company did not provide for such review. CAO finds this to be inconsistent with IFC's commitment to having clients manage E&S risks in accordance with the Performance Standards as set out in the Sustainability Policy (2006).

To harmonize the procedures for participating in rights issues with the higher level goals of the Sustainability Policy, IFC would need to ensure that appropriate consideration of the current status of a client's E&S obligations and compliance is required before rights issues are processed. Consideration of E&S risk prior to participation in rights issues will be particularly important in relation to: (a) projects that extend over a significant period of time; (b) projects which are operating under superseded E&S requirements; and (c) projects where E&S risk increases over time due to the changing nature of a business activity (such as when an early equity mining investment progresses towards development). While circumstances may exist that justify participation in a rights issue with regard to a project that has no or outdated E&S requirements, or where E&S performance is seriously deficient, following the 2006 Sustainability Policy, CAO would expect that this would be the exception and require specific justification from IFC.

Divestment

Unlike a loan which is repaid according to a pre-agreed schedule, IFC must take an active decision to divest from a project in which it holds an equity stake. IFC's Operational Procedures require an analysis of whether the investment's purpose has been "substantially fulfilled" prior to divestment. In circumstances where IFC's additionality is framed in terms of E&S issues (as was the case in relation to Quellaveco), this requires an analysis of E&S achievements and future risks. CAO finds no evidence that such analysis informed IFC's decision to divest from the Company.

CAO finds that it would be consistent with both the Operational Procedures on Equity Sales and IFC's broader commitments to E&S sustainability for E&S considerations to be structured in to IFC's decision making around divestment. This would allow IFC to determine whether a project has significant outstanding E&S risks, and determine how these should best be managed in the context of a potential divestment. In practice this might mean a requirement to analyze the current state of E&S obligations and compliance, and take this into account when making the decision to divest. Reference to the current status of E&S compliance, and the approach taken by IFC to mitigating post divestment E&S risk might also be required in the Equity Sale Memorandum.

In conclusion, CAO acknowledges steps taken by IFC E&S staff to supervise emerging risk in relation to the Quellaveco project, despite IFC's investment being made outside the framework of its E&S requirements. At the same time, CAO finds that a more robust framework for considering E&S issues when decisions were made in relation to rights issues and divestment may have put IFC in a better position to respond to the issues raised by the complaint.

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 the private sector lending and insurance members of the World Bank Group, the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (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 IFC and MIGA.

CAO compliance oversees investigations of the environmental and social performance of IFC and MIGA, particularly in relation to sensitive projects, to ensure compliance with policies, standards, guidelines, procedures, and conditions for IFC/MIGA involvement, with the goal of improving IFC/MIGA environmental and social performance

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

Acronyms

BTO	Back to Office
CAO	Office of the Compliance Advisor Ombudsman
CES	Environmental and Social Development Department [at IFC]
EA	Environmental Assessment
E&S	Environmental and Social
EHS	Environment, Health and Safety
EIA	Environmental Impact Assessment
ESMS	Environmental and Social Management System
ESRD	Environmental and Social Review Document
ESRS	Environmental and Social Review Summary
ESRP	Environmental and Social Review Procedure
ESRR	Environmental and social Risk Rating
IFC	International Finance Corporation
MIGA	Multilateral Investment Guarantee Agency
MOR	Monthly Operations Report
PDS	Project Data Sheet
PS	Performance Standards
PSR	Project Supervision Report
RAP	Resettlement Action Plan
SPI	Summary of Proposed Investment
TOR	Terms of Reference

1. Overview of the CAO Compliance Process

CAO's approach to compliance is set out in its Operational Guidelines (March 2013).

When CAO receives an eligible complaint, it first undergoes an assessment to determine how CAO should respond. If the CAO compliance function is triggered, CAO will conduct an appraisal of IFC's/MIGA's involvement in the project, and determine if an investigation is warranted. The CAO compliance function can also be triggered by the World Bank Group President, the CAO Vice President or senior management of IFC/MIGA.

CAO compliance investigations focus on IFC/MIGA, and how IFC/MIGA assured itself of project environmental and social (E&S) performance. The purpose of a CAO compliance investigation is to ensure compliance with policies, standards, guidelines, procedures, and conditions for IFC/MIGA involvement, and thereby improve E&S performance.

In the context of a CAO compliance investigation, at issue is whether:

- The actual E&S outcomes of a project are consistent with or contrary to the desired effect of the IFC/MIGA policy provisions; or
- A failure by IFC/MIGA to address E&S issues as part of the appraisal or supervision resulted in outcomes that are contrary to the desired effect of the policy provisions.

In many cases, in assessing the performance of the project and implementation of measures to meet relevant requirements, it is necessary to review the actions of the IFC client and verify outcomes in the field.

CAO has no authority with respect to judicial processes. CAO is neither a court of appeal nor a legal enforcement mechanism, nor is CAO a substitute for international court systems or court systems in host countries.

Upon finalizing a compliance investigation, IFC/MIGA is given 20 working days to prepare a public response. The compliance investigation report, together with any response from IFC/MIGA is then sent to the World Bank Group President for clearance, after which it is made public on the CAO website.

In cases where IFC/MIGA is found to be out of compliance, the CAO keep the investigation open and monitors the situation until actions taken by IFC/ MIGA assure the CAO that IFC/MIGA is addressing the non-compliance. The CAO will then close the compliance investigation.

2. Background to the Investment

2.1 Investment

The Quellaveco mining concession is located in Peru in the Region of Moquegua. It is an undeveloped porphyry copper deposit. It was privatized and acquired by Empresa Minera de Mantos Blancos SA (Mantos Blancos) in February 1993. At the time, the majority of Mantos Blancos' share capital was held by Anglo American Corporation of South America. Mantos Blancos established Minera Quellaveco SA (the Company) as a substantially wholly-owned subsidiary and assigned the Quellaveco mining concession to the Company.

In April 1993, the IFC Board approved an equity investment of \$6.2 million in the Company to fund a 20 percent share of acquisition costs and a two-phase feasibility pilot program for a technology assessment to confirm process feasibility and commercial viability. At the time, IFC described the likelihood of the Project leading to a commercial development as 'high' with the expectation that the construction of a mine could begin as soon 1997.²

Subsequent to IFC's investment the development of the mine was delayed. During the 1990s and 2000s, IFC participated in a number of rights issues with the result that by 2012 it had an 18.1 percent stake in the Company. Of the total of US\$59.8 million IFC committed to the Project, US\$46.9 million or 78.5 percent was committed after IFC adopted the 2006 Performance Standards (PSs). Details of these rights issues are set out in Annex 2 and discussed below. In February 2012 IFC sold all of its shares in the Company to a wholly-owned subsidiary of Mitsubishi Corporation. The remaining shares are held by Anglo American Quellaveco SA, now a wholly-owned subsidiary of Anglo American plc.

Quellaveco's copper reserve is estimated at 10 million tonnes (content metal basis) with an estimated mine life of 28 years. The initial production is expected to be approximately 225,000 tonnes per annum. The proposal to construct the mine is to be considered by Anglo American plc's board in 2015.³

² IFC (March 1993) *Quellaveco Board Paper (Proposed Investment)* p.1.

³ 'Anglo American expects turnaround plan to bear fruit in 2015' (Financial Times, 12 December 2013).

2.2 Project Timeline

Date	Milestone, Events and Documents
1993	
March	IFC Board - Approves equity investment in Quellaveco to support a two phase feasibility program with E&S category B. Board document provides that the Project will comply with applicable World Bank EHS Guidelines. Completion of feasibility work and commencement of mine construction flagged within 5 years. Likelihood of mine development described as "high".
June	IFC & Quellaveco – Enter into Shareholders Agreement without binding E&S requirements (IFC acquires 20% equity stake in Quellaveco for US\$6.22m).
1995	
January	Quellaveco – Completes Phase I of feasibility project.
1996	
March	IFC Board – Approves participation in rights issue of US\$5.3m (for a revised and enlarged program of feasibility work). Phase II feasibility work included studies to support the design of the mine, as well as securing required land and water rights.
1997	
September	Quellaveco – Submits EIA (EIS). IFC reviews and comments with reference to IFC E&S standards flagging concerns related to water supply, Indigenous Peoples (IPs), and stakeholder engagement.
1998	
December	IFC Annual Supervision Report– Identifies key E&S issues (safety of dams, resettlement, Indigenous People and water supply). Suggests that Quellaveco is receptive to IFC comments on E&S issues. Describes project as E&S category C.
1999	
December	IFC BTO Report – Discusses supplementary information needed to fulfill IFC requirements with a focus on issues of water supply, the requirements for the tailings dam and land acquisition.
2000	
February	IFC - Informs Quellaveco that the EIA (EIS), which has been developed for the purposes of local regulatory approval will not be sufficient for IFC purposes. Additional requirements including a Resettlement Action Plan (RAP), an IP Development Plan, and a Consultation and Disclosure Plan are noted.
June	IFC and CAO - Receive letters from local civil society organizations raising concerns regarding the negative impact of the proposed mine on water.
August	Government of Peru - Approves EIA and feasibility study (49 comments provided).
2001	
January	IFC - Delegated approval for participation in pre-emptive rights issue of \$750,000.
2003	
May	IFC - Determines not to subscribe to further rights issues.
2006	
April	Quellaveco - Unable to develop mine with original design (in particular, subterranean water sourcing plan).
October	IFC – Assigns E&S risk rating (ESRR) of 'A1-Good', indicating that this is considered category A project. The basis for this rating is unclear (no qualitative notes). Internal IFC correspondence from Sept. 2006 describes the Project's area of influence as well as potential cumulative impact as much greater than expected.

Date	Milestone, Events and Documents
2007	
March	IFC - Decides to meet previous cash calls to maintain stake at 18%.
November	IFC BTO Report - Describes forthcoming rights issue as category A. Reviews project against 2006 PSs identifying gaps. These include the absence of Stakeholder Engagement Plan and concerns regarding land acquisition and economic displacement of indigenous Aymara shepherds simultaneously with the preparation of a social baseline and a Resettlement Action Plan.
2008	
July	IFC Board - Approves exercise of pre-emptive rights in Quellaveco, US\$12m. Use of funds includes land acquisition, updates of studies and contributions to ongoing business expenditure.
2009	
March	IFC Project Supervision Report - Refers to a proposed amendment to the Shareholders' Agreement, noting that IFC's commitment of additional capital will be conditioned on Anglo's commitment to comply with IFC's PS.
2010	
March	IFC Project Supervision Report - Notes that amendment to Shareholders Agreement is no longer being pursued.
May	IFC Board - Approves exercise of pre-emptive rights in Quellaveco, US\$18m. Project substantively the same as that in July 2008 Board Paper.
November	IFC BTO Report - Reviews project performance against 2006 PSs, identifying material shortcomings. Notes the absence of an ESMS appropriate for construction (which at that stage was expected to start in early 2011). Recommends independent reviews in relation to key elements of the design, including the risk of groundwater contamination, and the design of the tailings dam. Identifies the urgent need to develop a comprehensive framework for managing resettlement to IFC standards, noting that land acquisition has been proceeding in advance of the development of adequate policies or planning.
2011	
January	IFC - Gives project ESRR of partly unsatisfactory (unsatisfactory in relation PS/Safeguards gaps).
March	IFC - Delegated approval for participation in pre-emptive rights issue of US\$5m.
March	IFC selects Mitsubishi Corporation as winning bidder for purchase of IFC's shares in Quellaveco. IFC and Mitsubishi proceed to due diligence and negotiation of final terms.
July	IFC - Delegated approval for participation in pre-emptive rights issue of US\$2.1m.
September	IFC - Delegated approval for participation in pre-emptive rights issue of US\$6m. IFC - Delegated approval for participation in pre-emptive rights issue of US\$3.8m.
November	CAO – Complaint received by CAO.
2012	
February	IFC and Mitsubishi sign an agreement on February 1, 2012 to sell IFC's entire interest in Quellaveco; sale completed on February 16, 2012.
March	CAO notifies IFC of the Complaint and CAO's decision that the complaint was eligible.

2.3 Developments since IFC's divestment

CAO understands that in March 2011, the regional government of Moquegua initiated a dialogue table comprised of 27 local stakeholders, including representatives of the company, civil society organizations, government representatives at the central, regional, municipal and district levels, and representatives of the following communities: Tumulaca, Pocata, Coscore and Tala.⁴ CAO also understands that some local officials from surrounding communities declined to participate in the dialogue process.

The records for the dialogue table available online indicate that in June 2011, the dialogue table was expanded after other stakeholders proposed looking at wider mining issues in the area, while still prioritizing Quellaveco as the first project to be discussed.⁵ Also in June, the dialogue table finalized the rules of engagement that would guide the process. CAO understands that in December 2011, other stakeholders took up protests against the Project and the dialogue table citing concerns about representation.

It is reported that on March 2, 2012, the Environmental Commission created within the dialogue process reached an agreement on alternatives regarding mine closure and remediation following cessation of mining operations at the proposed Quellaveco mine. The parties agreed that at mine closure, two thirds of sterile materials would be returned to the open pit, with the purpose of partially remediating the landscape as well as lowering risk of water contamination, and that the Asana River would be re-routed to its original course.

It is also reported that the dialogue process's Commission on Water Resources made some progress, including an agreement to hire a consultant to carry out a revision of the hydro-geological study of the open pit. A third Commission on Social Responsibility has also been created.

The material available indicates that the dialogue participants have met over 30 times since it was first convened. As of October 2013, the process was ongoing.⁶

Anglo American announced on December 12, 2013, that it has decided to delay the Quellaveco investment decision until a new feasibility study is completed in the next 12-18 months.⁷

At the time of writing approval for the development of the mine was pending.

⁴ <http://www.regionmoquegua.gob.pe/web13/lateral/contenido/mesadedialogo.html>.

⁵ <http://www.regionmoquegua.gob.pe/web13/lateral/contenido/mesadedialogo.html>.

⁶ <http://www.regionmoquegua.gob.pe/web13/lateral/contenido/mesadedialogo.html>

⁷ <http://www.angloamerican.com/~media/Files/A/Anglo-American-Plc/investors/presentations/2013pres/analyst-presentation-transcript-12-december-2013.pdf>

3. Background to the CAO Compliance Process

3.1 Complaint

In November 2011, CAO received a complaint from *Asociación Civil Labor*, a local environmental NGO in Peru, raising concerns about the Project's actual and anticipated impacts on local people and the environment. On CAO's request for documentation verifying the participation of project-affected groups, the Water Users Board of Moquegua and the *Frente Unificado de Defensa de los Intereses del Distrito de Torata* sent letters to CAO in March 2012. Given that the complaint was filed before IFC divested from the Project, CAO concluded that the complaint was eligible.

Based on the letters of complaint and the CAO Ombudsman Assessment Report,⁸ the issues raised in the complaint can be summarized as concerns regarding:

- (e) water scarcity, the degradation of water quality, and increased competition over water resources in an arid area;
- (f) pollution, including disposal of mine tailings and consequent environmental and health risks;
- (g) land claims on the Project sites; and
- (h) adequacy of community engagement, including lack of consultation on the initial and modified Environmental Impact Assessment.

CAO notes that key issues raised by the complainants (including those regarding the impact on water and possible pollution) relate to the prospective design, development and operation of the mine rather than to specific actions taken during the feasibility stage. These issues, however, remain relevant at the feasibility stage of the mine to the extent that they were or ought to have been addressed in the Company's process of environmental and social assessment as required by PS1.

3.2 Ombudsman Assessment Report

A CAO Ombudsman Assessment Report was published in July 2012.⁹ The Assessment Reports sets out that:

the local complainants were willing to sit down with the company for an initial engagement convened by CAO, the complainants did not expect to see their concerns resolved through such an engagement, but rather intended to use the opportunity to explain to the company why they see the Project as socially and environmentally unviable. Some complainants have since expressed an interest in deeper engagement with the company (p.8)

It also describes the company's position, namely that:

given the IFC's exit from the Project, and the existence of an ongoing dialogue process convened by local government that already substantively addresses many of the issues presented in the complaint to the CAO, it prefers to continue to work through the existing dialogue process than to see the CAO engage in a dispute resolution process (p.8-9).

⁸ http://www.cao-ombudsman.org/cases/case_detail.aspx?id=185.

⁹ http://www.cao-ombudsman.org/cases/case_detail.aspx?id=185.

As a result it was determined that the complaint should be sent to CAO Compliance for appraisal.

3.3 Summary of findings from the CAO Compliance Appraisal

CAO completed a Compliance Appraisal in accordance with its Operational Guidelines in May 2013.

The CAO Compliance Appraisal found that relevant E&S procedures and guidelines were referenced in the documentation that went to the IFC Board of Directors for the initial investment. However, the Company did not make any formal commitment to comply with E&S guidelines. The reasons for this are unclear. Documents provided to the IFC Board in the context of subsequent rights issues asserted inaccurately that the original 1993 investment was required to meet the World Bank Environmental standards then applicable, however, no such requirements are included in the 1993 Shareholders Agreement which provided the legal framework for IFC's investment in the Company.

In relation to supervision, the CAO Compliance Appraisal found that efforts were made to supervise the Company's compliance with IFC E&S standards as they evolved. In practice this meant that IFC E&S staff supervised the Project with regard to E&S impacts arising in the context of land acquisition and resettlement, the impact on Indigenous Peoples and the adequacy of public consultation. Significant attention was also paid to anticipated E&S impacts, including issues around water quality and access, pollution and cultural property. However, the Compliance Appraisal found that the lack of a contractual framework of E&S obligations made it difficult to address E&S concerns (for example those around land acquisition) which emerged during supervision.

The Compliance Appraisal also noted that project documentation that went to the Board during the course of supervision referred to the exploration activities being fully compliant with the Performance Standards and applicable guidelines, despite E&S supervision documents raising concerns about potential non-compliance with the Performance Standards, in particular PS5 (Land Acquisition and Resettlement) in 2007.

Finally, the Compliance Appraisal found that a review of certain aspects of this Project which relate to its nature as an early equity mining investment might better inform the application of policies (or other Compliance Investigation criteria) to future projects. CAO therefore decided to conduct a Compliance Investigation into the Project, having regard to the matters raised in the complaint, with a focus on the following questions:

- Are IFC's policies and procedures regarding environmental and social categorization of projects, as applied to its investment in Quellaveco, effective to reflect the magnitude of project risks and impacts?
- Are IFC's policies and procedures in relation to rights issues, as applied to its investment in Quellaveco, consistent with IFC's commitment to ensure that the business activities it finances are implemented in accordance with relevant environmental and social standards?
- Do IFC's policies and procedures regarding divestment from projects, as applied to its investment in Quellaveco, ensure appropriate consideration of environmental and social aspects prior to exiting?

The above framework formed the basis for the terms of reference for this CAO Compliance Investigation (see Annex 4). The terms of reference also required CAO to answer more general questions about how IFC assured itself of project environmental and social performance at appraisal and during supervision, and to articulate the immediate and underlying causes for any non-compliance identified.

3.4 Methodology

This investigation was conducted in accordance with the CAO Operational Guidelines (2013) with inputs from CAO staff and an expert panelist. From June to September 2013, the CAO team reviewed a range of relevant documentation. The team also conducted interviews with IFC management and staff who had direct knowledge of the Project.

Given the stage of development of the Quellaveco mine (not yet approved for construction at the time of writing), the alleged impacts are largely prospective. As such, the CAO Compliance Investigation process has focused on the adequacy of IFC's due diligence in its review and supervision of E&S aspects of the Project. In these circumstances, CAO determined that it was not necessary to conduct a field visit for the purpose of preparing this Investigation Report.

4. Investigation Findings

4.1 Introductory issues

IFC policy and procedures

The relevant environmental and social policy at the time the original investment in the Company was made was the Internal Procedure for Environmental Review of IFC Projects, which came into effect in December 1992. This Procedure was revised in October 1993. In September 1998, IFC approved a version of the Procedure which required compliance with IFC Environmental and Social Safeguard Policies, based closely on the World Bank Safeguards.

In April 2006, following fundamental restructuring and revision, IFC approved its Policy on Social and Environmental Sustainability (Sustainability Policy) which required client compliance with a new set of Performance Standards. In January 2012, IFC approved a new Sustainability Framework, incorporating an updated Sustainability Policy and Performance Standards.

For reasons set out in the CAO Compliance Appraisal, the 2006 and 2012 versions of the Sustainability Policy are treated as applicable to IFC's supervision of its Quellaveco Investment from April 30, 2006 and January 1, 2012 respectively.¹⁰

IFC's approach to early equity mining investments

IFC's Mining Group provides equity and loan financing for mining companies. It aims to combine financing with industry expertise and assistance in maximizing the social benefits of mining while minimizing its environmental footprint. IFC states that "[u]nder our unique Early Equity Program, we support mining projects at the pre-feasibility stage by becoming a shareholder and long-term partner."¹¹

An IFC brochure titled *Mining – Exploration Stage Equity* prepared in 2010 further explains IFC's approach to early equity mining investment.¹² It states that "IFC adds value to pre-feasibility stage mining projects by committing equity capital and providing hands-on help in managing environmental, social, and regulatory risks." It states that "IFC is a long-term equity investor, giving clients the space to focus on long-term growth." In relation to preparing for project finance, it states:

Our partnership with clients at the pre-feasibility stage often leads to additional IFC financing as projects progress. We offer financial products designed for all stages of project life cycles, including pre-IPO equity, quasi-equity, project finance loans, and syndication. Developing a project in line with IFC's environmental and social standards also prepares the ground to raise financing from other financial institutions at the project development stage.¹³

¹⁰ CAO, Appraisal for Compliance Investigation of IFC – Quellaveco (May 15, 2013), p6-7.

¹¹ IFC External Website - Industries > Oil, Gas & Mining > Sectors > Mining
http://www.ifc.org/wps/wcm/connect/industry_ext_content/ifc_external_corporate_site/industries/oil,+gas+and+mining/sectors/mining

¹² IFC Brochure, *Mining – Exploration Stage Equity: Mining Companies Face Many Risks – Let IFC Shoulder Some of Them* [IFC Intranet]
[ifcnet.ifc.org/intranet/coc.nsf/AttachmentsByTitle/Mining+Exploration/\\$FILE/MiningExploration+m.pdf](http://ifcnet.ifc.org/intranet/coc.nsf/AttachmentsByTitle/Mining+Exploration/$FILE/MiningExploration+m.pdf)

¹³ *Ibid.*

In the course of this compliance investigation, IFC staff confirmed that investing in early equity mining projects provides an opportunity for IFC to build the capacity of small exploration companies, providing resources and assisting in the establishment of an E&S management system. It was also explained that early involvement also allows IFC to provide input on the TOR for Environmental and Social Impact Assessments, ensuring that they are prepared in accordance with the Performance Standards.

IFC staff also confirmed that from a value and developmental perspective, IFC selects projects with the aim of converting to production or selling to operators that can produce. However on a portfolio basis, it expects that a significant number will not progress to production because exploration results are not satisfactory.

Quellaveco was majority owned by a company closely related to Anglo American plc. In the documentation CAO reviewed, and in interviews with IFC staff, emphasis was placed on Anglo American's corporate commitment to environmental and social standards for their operations, including reference to IFC's Performance Standards.¹⁴ Anglo American's corporate commitments notwithstanding, it was understood that IFC had a role to play in helping to ensure best practice in social and environmental aspects of the Project. This was confirmed by site visits undertaken by IFC E&S staff towards the end of the investment, one of which noted that IFC could possibly play a beneficial role in integrating Anglo's international office and policies with the local office.¹⁵

4.2 Environmental and social categorization

The first issue identified in the terms of reference is whether IFC's policies and procedures regarding environmental and social categorization of projects, as applied to its investment in the Company, are effective to reflect the magnitude of project or business activity risks and impacts. This requires consideration of the categorization policy at the time when IFC invested, how this policy has changed over time, guidance for its application generally, and the particular application of the policy to IFC's investment in the Company.

Categorization policy and guidance

According to IFC's 2012 Sustainability Policy, the purpose of IFC's process of environmental and social categorization is "to reflect the magnitude of risks and impacts" of a project.¹⁶ The category of a project also determines IFC's institutional requirements for disclosure.

This process of categorization was in place when IFC made its initial investment in the Company. The 1992 Internal Procedure for Environmental Review of IFC Projects provided that:

Early in the review process all IFC projects are categorized by the Environment Unit into one of the following four categories based on their potential environmental impact, and thus the required level of environmental analysis:

Category A Projects – may result in diverse and significant environmental impacts, thus requiring a detailed Environmental Assessment (EA).

Category B Projects – may result in specific environmental impacts and require adherence to certain predetermined performance standards, guidelines, or design criteria to mitigate impacts.

¹⁴ Anglo American (2009) *The Anglo Social Way – Management Systems Standards*.

¹⁵ IFC, *ESRD (BTO incorporated)* (November 2007).

¹⁶ IFC (2012) *Policy on Environmental and Social Sustainability*, para. 40.

These projects do not normally require preparation of a detailed environmental assessment, but an environmental analysis is required. A wide range of environmental guidelines have been developed by local or country authorities, as well as by a number of organizations, including the World Bank Group. In addition, specific environmental design criteria can be developed for individual projects.

Category C Projects – normally do not result in any environmental impact and thus do not require any further environmental review.

Financial Intermediary (FI) – may include financing a variety of subprojects that may result in environmental impacts, thus requiring environmental review by the financial intermediary, in accordance with this IFC procedure.¹⁷

While the definition of each category has been developed with new iterations of IFC's environmental and social policy, the core categories have not changed significantly since they were first defined (see Annex 3). Since 2006, however, categorization has substantially been de-linked from procedural requirements relating to IFC's environmental and social due diligence, and from the tools IFC requires clients to apply to assess impacts. IFC staff interviewed by CAO emphasized that in their view there is procedurally little difference between the approach IFC takes to a category A project contrasted with a category B project. However, categorization may still have practical consequences, particularly for disclosure.¹⁸

The application of the current policy on categorization is guided by an Interpretation Note on Environmental and Social Categorization.¹⁹ Parts of this note are incorporated into the April 2013 update of the Environmental and Social Review Procedures (ESRP) chapter on Direct Investments: Pre-Mandate Initial Review, Concept Review Meeting, and E&S Specialist Assignment. This guidance reflects significant developments in IFC's approach to categorization since its original investment in the Company.

The Interpretation Note indicates that where the use of IFC financing and the associated E&S footprint of the business activity are known or largely known at the time of the decision to invest, IFC will determine the business activity's E&S category based on E&S risks and impacts. The approach to categorization "will include the assessment of inherent risks related to the sector of operation, as well as the context of the business activity's likely geographic setting."²⁰

The Interpretation Note also addresses the situation where the use of IFC financing and/or the E&S footprint of the business activity cannot be well understood or defined at the time IFC undertakes E&S due diligence. In these circumstances, "IFC will determine the E&S category based on risks inherent to the particular sector, as well as on the likelihood of a development taking place and on what can be reasonably known about the environmental and social characteristics of the business activity's likely geographical setting."²¹ The Note explains the application of this interpretation as follows:

¹⁷ IFC (1992) *Internal Procedure for Environmental Review of International Finance Corporation Projects*, para. 8.

¹⁸ For example, Category A projects must be disclosed no less than 60 days prior to consideration of the investment by IFC's Board of Directors, whereas Category B projects must be disclosed no less than 30 days prior to consideration of the investments by IFC's Board of Directors.

¹⁹ IFC (2012) *Interpretation Note on Environmental and Social Categorization*.

²⁰ *Ibid.* para. 9.

²¹ *Ibid.* para. 11.

investments which involve sectors that are of inherent high risk and are expected to be located in sensitive environmental areas or areas with significant social disruption will be categorized as A. Investments in sectors of inherent high risk but likely located in lower E&S risk settings will be categorized as A or B depending on availability of specific information. For instance, when IFC's investment is not related to any specific activities which would increase the company's footprint (e.g., financial restructuring or liquidity support) or financed activities which are within existing footprint (e.g., brownfield) or financed activities which are for exploratory/investigative work, the IFC's investment would typically be categorized as B.²²

In an interview with CAO, E&S IFC staff indicated that an early equity mining project would only be categorized A if there was a particularly high risk element in the exploration stage process, such as if exploration was to occur on the edge of critical habitat, or if Indigenous Peoples were potentially adversely affected.

The 2012 Sustainability Policy recognizes that the risk profile of an investment may change over time. To address these situations, the 2012 Policy "requires that clients inform IFC when there is a material change in their businesses or when they plan to enter into a new business area that is materially different from what was represented when IFC obtained Board approval."²³ In this context, "[m]aterial change may include change in environmental and/or social risk profile."²⁴ On being notified of a material change, "IFC will assess whether the new business area poses environmental and/or social risks and/or impacts, and if so, IFC will require the client to adjust its Environmental and Social Management System ... in a manner consistent with (i) potential environmental and social risks and impacts associated with material changes of these new businesses; (ii) this policy; and (iii) applicable requirements of the Performance Standards."²⁵ The Interpretation Note indicates that the requirements regarding material change "will not affect the E&S category assigned to the original investment as IFC's institutional disclosure has already taken place."²⁶

The policy relating to the categorization of rights issues has changed over time. Under the 1998 Procedure for Environmental and Social Review of Projects, rights issues were considered category C on the basis that they were likely to have minimal or no adverse environmental impacts. Since 2007, the ESRP has provided that for rights issues, the project E&S category should remain the same as the original investment E&S category.

The April 2013 update of the ESRP chapter on Direct Investments: Pre-Mandate Initial Review, Concept Review Meeting, and E&S Specialist Assignment sets out a table of "Transactions that do not require due diligence," stating that "[E&S] Specialists are not typically engaged in the special investment instruments listed below." "Rights issue" is listed as one of the investments not requiring due diligence.²⁷ The ESRP states "[n]o further action is necessary in these cases, but if so required automated categorization can be overridden and a revised category can be assign[ed]" by IFC E&S Department (CES).²⁸ It is not clear what is intended by this provision, but it was suggested to CAO by IFC that this might provide scope for a change in categorization

²² *Ibid.*

²³ *Sustainability Policy* (2012), para. 25.

²⁴ *Ibid.*

²⁵ *Ibid.*

²⁶ *Interpretation Note* (2012) para. 8.

²⁷ *ESRP* (April 2013) para. 2.5.

²⁸ *Ibid.*

where a rights issue is used as a vehicle to support the transition of a mining project from exploration to development and/or construction.

The logic of having rights issues follow the categorization of the original project is not always clear, particularly when the E&S risk profile of a project changes over time. The reference in the April 2013 Update of the ESRP discussed above, which allows for automated categorization for rights issues to be “overridden” and a “revised category” assigned by IFC CES, may permit exceptions to the general rule that categorization of a rights issue follows categorization of the original project. Given the objectives of IFC’s E&S categorization, and the fact that the risk profile of an early equity mining project may change significantly over time, clarification of the procedures for categorization of rights issues may be required.

Application of categorization policy to Quellaveco

IFC’s Initial Project Review, prepared in January 1993, stated that the feasibility/pilot project would be a category B project, while the mine development program would be category A.²⁹

Minutes of a Decision Meeting held on March 12, 1993 reiterated that the Project consisted of a two-phase feasibility/pilot program to carry out a technology assessment to confirm process feasibility. Phase I would involve ore sampling, further definition of the well-explored ore reserves, larger lab-scale tests and conceptual engineering. Phase II would involve the operation of heap leaching tests, pilot plant testing at the mine site, mine planning, detailed engineering, and feasibility studies including an Environmental Assessment Study.

Language proposed by the IFC Environment Unit was incorporated into the IFC Board Paper, which confirmed that the two phase feasibility/pilot project would be a category B project whereas the potential mine development program expected to result from the feasibility/pilot project would be category A.³⁰

An ESRR prepared by IFC E&S staff in October 2006, however, identified the investment as category A. In November 2007, IFC E&S staff prepared a detailed Environmental and Social Review Document (ESRD) for a proposed rights issue combined with a BTO review of the existing equity investment. This report also referred to the provisional categorization for the proposed rights issue as A, with the rationale provided that it “must be same as original project.” IFC has informed CAO that these references to the Project being category A were incorrect.

The paper prepared for the Board on a Proposed Exercise of Pre-Emptive Rights in the Company, dated July 1, 2008, stated that “IFC’s original investment was a category B project, and this rights issue is also a category B under IFC’s environmental procedures.”³¹ This accords with the direction that the project E&S category for rights issues should remain the same as the original investment E&S category. Similarly, the paper prepared for the Board on a Proposed Exercise of Pre-Emptive Rights in the Company, dated May 11, 2010 stated that:

IFC’s original investment was a category B project since it was only to fund exploration and feasibility studies which caused no significant impacts. This rights issue is also a category B as specified in IFC’s operational procedures (rights issues always follow the categorization of the original investment).³²

²⁹ IFC (January 1993) *Initial Project Review – Peru: Quellaveco Copper Project*, p.1.

³⁰ *Quellaveco Board Paper* (1993) p.3.

³¹ IFC (July 2008) *Quellaveco Board Paper (Proposed Exercise of Pre-Emptive Rights)*, p.8.

³² IFC (May 2010) *Quellaveco Board Paper (Proposed Exercise of Pre-Emptive Rights)*, p.9.

Conclusion

CAO has concerns that the manner in which categorization policies and procedures are applied by IFC in the context of early equity mining projects does not support the articulated objectives of E&S categorization.

During discussions with IFC, there was some suggestion that categorization is ultimately irrelevant (other than in terms of pre-Board disclosure requirements) and has no impact on how IFC approaches the assessment of risks and impacts and the way they are mitigated. IFC staff advised that the main difference between an A and a B project is whether 60 or 30 days' notice is required before a project is considered by the Board. It was suggested that community expectations of an operational mining project might be raised unnecessarily if exploration projects were categorized A rather than B, as at this stage no decision has been reached as to whether to proceed with an operational mine.

Categorization plays a central role in providing an accurate reflection of the magnitude of risks and impacts of a project, and in signaling those risks and impacts to various stakeholders. Public awareness of the environmental and social risks and impacts associated with an IFC-funded project is determined, to a significant extent, by the category IFC assigns to the project. Regardless of the limited procedural implications from IFC's perspective, it is therefore important that IFC projects are accurately categorized.

In applying categorization policies and procedures to an early equity mining project, IFC focuses on the particular activities that will be financed. Current practice on categorization does not take into account the purpose of the investment, which for the early equity business line is (subject to viability) the development of a mine.

While activities financed by IFC in an early equity mining project may be limited, the nature of the investment means that IFC is taking an equity stake in a company which is dedicated to the development of a mine. In a project such as Quellaveco, where the prospects for commercial development are held out by IFC as being high, CAO finds that applying an E&S classification of B takes an unduly narrow view of project risks and impacts.

These concerns would be addressed most clearly if IFC provided guidance that, in certain circumstances, early equity mining investments should be categorized as A. The decision as to whether an early equity mining project should be categorized as A or B would need to be determined on a case-by-case basis, taking into account the potential E&S impacts of the project (both immediate and long term), as well as its likelihood of development.

This approach would be consistent with IFC's stated goal (of being a long term investor). This approach is also consistent with the wording of the Sustainability Policy and accords with current guidance that the E&S category is to be determined considering risks inherent to a particular sector, the likelihood of a development taking place, and what can reasonably be known about the environmental and social characteristics of the business activity's likely geographical setting. Applying this approach to categorizing early equity mining projects could also assist IFC and its clients in engaging with project-affected communities over the course of what are likely, in the long-term, to be high-risk projects.

In addition, these concerns would be addressed if IFC provided guidance about re-categorization of projects. Currently, CAO finds that IFC policy guidance for the re-categorization of projects is unclear. Re-categorization allows IFC to publicly signal changing (or developing) risk and impact profiles for IFC projects. The only guidance on re-categorization of

projects is found in the April 2013 update of the ESRP chapter on Direct Investments: Pre-Mandate Initial Review, Concept Review Meeting, and E&S Specialist Assignment. It would be useful to have a clear process for re-categorization of projects, together with an identification of circumstances that may trigger re-categorization (such as completion of an ESIA that identifies potential significant adverse environmental or social risks and/or impacts that are diverse, irreversible or unprecedented).

In relation to Quellaveco, CAO notes supervision documentation prepared by IFC E&S staff which indicate that Indigenous People were potentially affected during the pre-construction stage of the Project, particularly through economic displacement in advance of adequate consultation and planning.³³ As such, the Project would appear to fall within the scope of projects involving a high risk element in the pre-construction phase. This suggests that, in any event, the Project should have been categorized A under IFC's interpretation of the existing Policy at the time of investment. In addition, CAO notes that in the case of Quellaveco, the longer-term impacts were considered likely to be diverse, irreversible or unprecedented, and at the time at which IFC invested, the likelihood of the Project proceeding to development was considered high.

4.3 E&S requirements around participation in rights issues

The second issue identified in the terms of reference is whether IFC's policies and procedures in relation to rights issues, as applied to its investment in Quellaveco, are consistent with IFC's commitment to "ensure that the projects it finances are operated in a manner consistent with the requirements of the Performance Standards."³⁴ This requires consideration of IFC procedures regarding rights issues over the time of the investment in the Company generally, and the particular application of the procedures to IFC's investment in the Company. It also requires consideration of the provision in the Sustainability Policy (2006) that "IFC does not finance new business activity that cannot be expected to meet the Performance Standards over a reasonable period of time."³⁵ The Sustainability Policy (2012) includes a similar, though broader, provision that "IFC will only finance investment activities that are expected to meet the requirements of the Performance Standards within a reasonable period of time."³⁶

Procedures on rights issues

IFC E&S procedures in relation to rights issues have developed over time. As noted above, under the 1998 Procedure for Environmental and Social Review of Projects, rights issues were considered category C on the basis that they were likely to have minimal or no adverse environmental impacts. As such, beyond screening, no further environmental assessment was required. The 2006 ESRP was silent on rights issues. The 2007 ESRP provides that

For projects where IFC's proposed financing is for Rights Issues where the subscription price for additional shares in each transaction exceeds ten million dollars (\$10,000,000), no review or public disclosure documents (SPI, ESRS) are necessary per IFC's Operational Procedures XI.2.³⁷

³³ IFC ESRD (*BTO incorporated*), (November 2007).

³⁴ *Sustainability Policy* (2006) para. 5.

³⁵ *Sustainability Policy* (2006) para. 17.

³⁶ *Sustainability Policy* (2012) para. 22.

³⁷ *ESRP* (2007) para. 2.2.2(d).

No rationale is provided for the establishment of the \$10m threshold. Nor is procedure provided for subscription prices below \$10m. The February and August 2009 ESRPs addressed rights issues in essentially the same terms as the 2007 ESRP.

The 2010 ESRP provides that:

For projects where IFC's proposed financing is for Rights Issues ... no review or public disclosure documents (Summary of Proposed Investment and Environment and Social Review Summary or Environmental and Social Clearance Memoranda) are necessary.³⁸

The April 2013 update of the ESRP chapter on Direct Investments: Pre-Mandate Initial Review, Concept Review Meeting, and E&S Specialist Assignment does not include an equivalent provision. As noted above, it provides that IFC E&S Specialists are not typically engaged in the process for preparation of a rights issue.³⁹

The procedure for processing rights issues is found in the IFC Operational Procedures: Portfolio Operations and Supervision Processes, Section XV. This states that IFC has delegated authority from the Board to exercise rights issues up to an aggregate ceiling amount for the fiscal year, provided the subscription value for each transaction does not exceed \$10m. Proposals to exercise rights issues with a subscription value of over \$10m are sent to the Board for approval under the No-Objection Procedure.

On the announcement of a rights issue, it is the Portfolio Officer's responsibility to recommend one of three possible courses of action: subscribe, sell the rights or do nothing (i.e. let the rights lapse). The authority to approve recommendations on rights issues generally lies with the relevant Regional Industry Portfolio Manager or the relevant Regional Industry Director.

The procedure for participating in a rights issue includes the preparation of a rights issue memorandum, clearance and approval. There is no requirement for consultation with IFC E&S staff.

In summary, there is no requirement for consultation to occur between IFC E&S staff and the investment team around IFC's decision whether to participate in a rights issue. Neither is there a requirement to provide an update on E&S issues to the Board in the context of a rights issue which goes to the Board.

It is clear that the E&S department has professional expertise and knowledge that may be relevant to IFC's participation in a rights issue. IFC has informed CAO that E&S staff may be consulted in the context of a rights issue, and that information about E&S issues may be included in material provided to the Board about a rights issue. However, such consultation appears to be ad hoc.

In discussions with CAO, IFC noted that the time period within which IFC is expected to respond to a rights issue is generally determined by the client, and may also be affected by whether the company in question is listed or unlisted. This may place some practical limitations on the scope for inquiry between IFC receiving a request to participate in a rights issue, and IFC's decision to

³⁸ ESRP (2010) para. 2.5.3.

³⁹ ESRP (April 2013) para. 2.5.

participate in a rights issue. IFC staff also noted that its equity interest will generally be diluted if it decides not to participate in a rights issue, potentially reducing its leverage.

Application of rights issues policy to Quellaveco

Between 1993 and 2012, IFC participated in a number of significant rights issues offered by the Company (set out in Annex 2). The total amount approved for rights issues amounts to US\$53.55m (in contrast to an initial investment of US\$6.22m). Between 2004 and 2007, IFC decided not to participate in rights issues, allowing its interest to be diluted. IFC staff informed CAO that IFC generally had 45 days from receipt of a request to participate in a rights issue to determine whether it would participate. Of the total of US\$59.8 million IFC committed to the Project, US\$46.9 million or 78.5 percent was committed after IFC adopted the 2006 Performance Standards.

The work carried out under the Project changed over this period of time, from phase 1 feasibility work in 1993 (ore sampling, definition of mineralogy and conceptual engineering) through to work preparatory to design and development, including land acquisition and resettlement later in the project cycle. The Project, however, remained in the feasibility and planning phase and had not at the time of divestment proceeded to construction. IFC E&S standards also developed significantly over this period of time, as outlined above. However, as noted in CAO's Compliance Appraisal, the legal agreement for this investment did not include E&S requirements.

IFC staff indicated to CAO that when IFC decided to re-engage with the Company and begin participating in rights issues in 2007, it undertook several missions including a review of E&S compliance. The results of these missions are summarized in the relevant IFC Board papers.

In correspondence with CAO, IFC staff indicated that commitment to the Performance Standards was included as part of a set of changes to the Shareholders Agreement which were proposed in advance of IFC recommencing its participation in the Quellaveco rights issues in 2010. IFC also explained that, over time, commercial circumstances shifted and IFC decided not to pursue the changes in the agreement as it seemed unlikely that they would find a common position given a lengthy negotiation that had led to no results. This description of events is supported by internal Credit Risk Rating reports prepared by IFC staff between 2008 and 2010.

IFC also indicated that while the Performance Standards were not applicable as a matter of contractual obligation, IFC staff nevertheless engaged with the Company on the Performance Standards and supervised the Project in accordance with the Performance Standards. In CAO's view, this was good practice.

The scope to negotiate changes to E&S obligations may depend upon the circumstances. For example, in 2007, IFC negotiated with the Company, having not participated in rights issues for a number of years, and in the context of there being only two shareholders. While this indicates possible leverage and scope to negotiate E&S obligations as part of the 2007 rights issue in relation to this particular investment, CAO acknowledges that this may not always be the case.

Conclusion

CAO finds that IFC complied with existing procedures for participating in rights issues in Quellaveco. However, IFC procedures for participating in rights issues as applied to Quellaveco, did not ensure consideration of whether the rights issues would fund "new business activity." To this extent, CAO finds that the procedures were inconsistent with para. 17 of the Sustainability Policy (2006), which implies a requirement to analyze any additional financing in terms of

whether it involves “new business activity”, and if so to apply the Performance Standards to that investment.⁴⁰ In relation to the Quellaveco rights issues, CAO finds while business activities developed over time, the change was not so significant as to be properly classified as “new business activity.” There was thus no breach of the Sustainability Policy in this respect.

More generally, CAO notes that there are significant risks involved in providing additional finance to a project that has inadequate or outdated E&S obligations, or where there is evidence of non-compliance with existing E&S obligations. Given these risks, consistency with IFC’s policy commitment to “ensure that the projects it finances are operated in a manner consistent with the requirements of the Performance Standards”⁴¹ would require IFC’s participation in a rights issue to be contingent upon an appropriate review of project E&S risk. IFC’s procedures as applied in the processing of rights issues for Quellaveco did not provide for such review. CAO finds this to be inconsistent with IFC’s commitment to having clients manage E&S risks in accordance with the Performance Standards as set out in the Sustainability Policy (2006).

To harmonize the procedures for participating in rights issues with the higher level goals of the Sustainability Policy, IFC would need to ensure that appropriate consideration of the current status of a client’s E&S obligations and compliance is required before rights issues are processed. Consideration of E&S risk prior to participation in rights issues will be particularly important in relation to: (a) projects that extend over a significant period of time; (b) projects which are operating under superseded E&S requirements; and (c) projects where E&S risk increases over time due to the changing nature of a business activity (such as when an early equity mining investment progresses towards development). While circumstances may exist that justify participation in a rights issue with regard to a project that has no or outdated E&S requirements, or where E&S performance is seriously deficient, following the 2006 Sustainability Policy, CAO would expect that this would be the exception and require specific justification from IFC.

4.4 E&S requirements around divestment

The third issue identified in the terms of reference is whether IFC’s policies and procedures regarding divestment from projects, as applied to its investment in Quellaveco, ensure appropriate consideration of environmental and social aspects prior to exiting. This requires consideration of relevant IFC policy regarding divestment generally, and the application of this policy to IFC’s particular divestment from the Company.

Policy on divestment

IFC’s Articles of Agreement state that

The Corporation shall seek to resolve its funds by selling its investments to private investors whenever it can appropriately do so on satisfactory terms.⁴²

⁴⁰ Note the *Sustainability Policy (2012)* para. 22 (the equivalent of the *Sustainability Policy (2006)* para. 17) refers more broadly to any “investment activities” rather than “new business activities” as being expected to meet the requirements of the Performance Standards, suggesting that IFC’s participation in a rights issue post January 2012 should be contingent on a determination that the investment will meet the requirements of the Performance Standards.

⁴¹ *Sustainability Policy (2006)* para. 5.

⁴² IFC, *Articles of Agreement*, Article III, Section 3(vi).

IFC's approach to equity sales is set out in its Operational Procedures.⁴³ These provide that the sale of IFC's equity investments "is dictated by IFC's interests" but also that in principle, "IFC will not seek to sell an equity investment before substantially fulfilling the investment's original purpose, unless the original objectives can no longer be achieved." The Operational Procedures provide that equity sales will be reported to the IFC Board through its Monthly Operations Report (MOR). The MOR is to include "reasons for the sale, confirming its consistency with the share sales policy."⁴⁴

CAO's discussions with IFC staff reflected an understanding that the decision to divest from a project may be taken for a range of reasons. IFC may divest because it stands to make a profit, or it may divest in order to minimize its losses. IFC may divest because its objectives have been achieved, or because of serious non-compliance with E&S requirements, where efforts to bring the Project back into compliance have failed. IFC's objectives include both financial and development objectives. IFC staff explained that E&S issues might be considered in the context of development objectives.

As explained to CAO by IFC staff, the Portfolio Manager and the Portfolio Officer will regularly review the Credit Risk Rating for projects within their portfolio, and may decide to recommend divestment. The Credit Risk Rating reports include reference to an ESRR. When a decision to divest is made, a recommendation memo is usually prepared by these officers. Once the sale is concluded, details are provided in the Monthly Operations Report to the Board.

IFC staff further explained that E&S issues are generally only considered in the context of divestment if issues of reputation and liability arise. In such circumstances, it was explained that discussions between the investment team and IFC CES staff would be expected. Generally, however, there would be no reason for IFC CES to be consulted when divestment was proposed. Engaging with CES in the context of divestment is clearly good practice when it occurs. However, there is apparently no requirement that this occur.

Regarding E&S considerations beyond IFC's involvement in a project, the 2006 Policy on Environmental and Social Sustainability states that IFC will "[e]ncourage the client to continue to meet the Performance Standards after IFC's exit from the project."⁴⁵ The 2012 Policy does not include an equivalent provision. However, it maintains IFC's commitments to "positive development outcomes" noting that that "an important component of achieving positive development outcomes is the environmental and social sustainability of these activities."⁴⁶

Application to Quellaveco

An Equity Sale Memorandum was prepared on January 11, 2012 by the Portfolio team for the relevant Vice President. The Memorandum sought approval to proceed with the proposed sale of 100 percent of IFC's shares in the Company, and noted that details would be reported in the next Monthly Operations Report to the Board.

The Memorandum records the approval status of the equity sale. It is clear that the sale was cleared by the Portfolio team, the Equity Department, the Legal Department, and the relevant Vice President. No reference is made in the Memorandum to the environmental and social

⁴³ IFC, *Operational Procedures: Portfolio Operations & Supervision Processes* (2014), para XIV.1.1.

⁴⁴ *Ibid.*, para. XIV.6.

⁴⁵ *Sustainability Policy* (2006) para.26.

⁴⁶ *Sustainability Policy* (2012) para.1.

status of the Project and no E&S staff were included in the clearance process. Nor is any reference made in the Memorandum to the divestment criteria discussed above, in particular the principle that “IFC will not seek to sell an equity investment before substantially fulfilling the investment’s original purpose, unless the original objectives can no longer be achieved.”⁴⁷

As noted above the objectives of IFC’s investments in Quellaveco included E&S elements. These are articulated in terms of supporting “project design, operations management and mineral processing [that] would be carried out in line with IFC’s E&S standards” and helping to “build the right foundation for Quellaveco to deal with E&S issues that will arise in the later phases of the Project.”⁴⁸

There is no indication that the investment team discussed divestment with IFC CES staff prior to divestment occurring, or otherwise considered E&S issues when making the decision to divest.

IFC included a note on the Quellaveco equity sale in its March 2012 Monthly Operations Report to the Board. The note describes the history of IFC’s investment and provides financial details of the sale. Reasons for the sale are not articulated, nor is there an analysis of whether the objectives of the original investment had been fulfilled. In relation to E&S issues the Monthly Operations Report does contain a statement that IFC expects Anglo and Mitsubishi to continue to take all necessary steps to progress the Project in a sustainable manner. As mentioned above, however, there is no indication that this statement was based on inputs from CES staff. On the contrary, the most recent inputs from CES staff (from January 2011) indicated that the Project’s E&S performance was partly unsatisfactory, with significant issues related to the adequacy of the client’s E&S Management System and gaps in compliance with relevant E&S standards.

Conclusion

IFC’s Operational Procedures on Equity Sales require an analysis of whether the investment’s purpose has been “substantially fulfilled” prior to divestment. In circumstances where IFC’s additionality is framed in terms of E&S issues (as was the case in relation to Quellaveco), this requires an analysis of E&S achievements and future risks. CAO finds no evidence that such analysis informed IFC’s decision to divest from Quellaveco or that it was reported to the Board.

More broadly, CAO finds that IFC’s Operational Procedures on Equity Sales do not adequately support IFC’s commitments to E&S sustainability in its investments. In relation to early equity investments, where IFC divests prior to the development of a mine, a lack of structured attention to E&S performance prior to divestment may mean that future impacts are inadequately mitigated. In a worst case scenario this could give rise to a situation where a project that IFC invests in causes significant social and/or environmental harm after IFC divestment. The question of how IFC should respond to this type of risk is not captured in the Sustainability Framework or associated procedures.

Further, CAO finds that it would be consistent with IFC’s Operational Procedures and IFC’s broader commitments to E&S sustainability for E&S considerations to be structured in to IFC’s decision making around divestment. This would allow IFC to determine whether a project has significant outstanding E&S risks, and determine how these should best be managed in the context of a potential divestment. In practice this might mean a requirement to analyze the

⁴⁷ IFC, *Operational Procedures* (2014), para XIV.1.1.

⁴⁸ *Quellaveco Board Paper* (2008) p.5f & (2010) p.6f.

current state of E&S obligations and compliance, and take this into account when making the decision to divest. Reference to the current status of E&S compliance, and the approach taken by IFC to mitigating post divestment E&S risk might also be required in the Equity Sale Memorandum.

5. Conclusion

General

In reaching conclusions on IFC's E&S performance in relation to Quellaveco, CAO recognizes that this investment was initiated at a time when IFC E&S procedures were relatively underdeveloped. In addition, because the Project was designed to support a series of feasibility studies, it was assumed that its E&S impact would be limited. Nevertheless, CAO finds that the absence of E&S requirements in IFC's Shareholders Agreement for Quellaveco meant that there was a significant gap in terms of the Company's E&S obligations, even as required under the 1992 procedure, and particularly given IFC's undertaking to its Board of Directors in March 1993 that the Project would "comply with all applicable World Bank environmental and occupational health and safety guidelines." CAO finds that the absence of E&S requirements in IFC's investment agreement made E&S supervision difficult. In making this finding CAO acknowledges IFC's position that supervision of the Project was thorough and took account of the evolving Performance Standards. In any event, CAO also acknowledges that the subsequent development of IFC's E&S policies and procedures, means that such an oversight should not occur today.

Notwithstanding the absence of E&S requirements, CAO finds that IFC supervised the Project with reference to IFC's evolving E&S standards and policies. During supervision, IFC identified a range of social concerns regarding land acquisition and resettlement, the Project's impact on Indigenous Peoples and the adequacy of public consultation. IFC also identified potential environmental impacts, including the adequacy of the water resources needed to service the mine, and the potential for water pollution. This represented good practice.

While the Complainants' concerns had not fully been addressed as at the time of IFC's divestment, CAO finds that IFC's engagement with the Company around E&S issues was generally appropriate to the stage of development of the Project. CAO notes IFC's view that the Company was broadly receptive to IFC advice on E&S issues. However, CAO also finds that key E&S issues identified by IFC in project supervision were not translated into corrective action plans. Agreeing on such plans would have been of particular relevance in relation to: (a) land acquisition activities (which IFC noted were proceeding in advance of the development of studies and plans required by Performance Standard 5); (b) the impact of land acquisition on Indigenous People, (c) issues of stakeholder engagement and (d) the more technical elements of project design and environmental impact assessment that are discussed in IFC's 2007 and 2010 supervision reports.

CAO also finds that certain information presented by IFC to its Board in the course of this Project was incomplete. This includes statements that: (a) the Project would comply with the World Bank's environmental standards (in a context where the legal agreement did not include such requirements);⁴⁹ and (b) exploration activities were "fully compliant with the Performance Standards,"⁵⁰ (in a context where IFC had documented gaps in compliance with the Performance Standards and was concerned about the readiness of its Client to further develop the Project in accordance with these Standards).

⁴⁹ *Quellaveco Board Paper* (1993); *Quellaveco Board Paper* (2010).

⁵⁰ *Quellaveco Board Paper* (2010) p.9.

In relation to this point, CAO notes IFC's view that concerns raised during supervision related to gaps that would need to be addressed in order to achieve future compliance with the Performance Standards, and were not indications of non-compliance at the time.⁵¹ In this context CAO notes references in IFC's 2007 supervision documentation indicating that land acquisition and as such impacts had begun in advance of the development of adequate compensation planning. CAO also notes references in IFC's 2007 supervision documentation that environmental and social studies were not necessarily being developed to IFC standards. Significant gaps in compliance with the Performance Standards, including ongoing concerns regarding Quellaveco's approach to land acquisition are confirmed in IFC's 2010 supervision documentation. It is on this basis that CAO finds IFC's 2010 statement to the Board that the Project was "fully compliant with the Performance Standards" did not represent a complete presentation of the information available to IFC.

More generally, this compliance investigation raises questions about IFC's application of the Sustainability Framework and associated procedures to the long-term E&S risk associated with early equity investments in the mining sector.

Categorization

In relation to categorization, it is clear that there are challenges involved in evaluating E&S risks in early equity mining projects. On one hand, if the feasibility work ultimately does not result in a decision to develop a mine, a project's potential E&S risks and impacts will be limited to the consequences of undertaking pre-construction activities. On the other hand, if a decision to proceed with development of a mine, particularly one in a socially or environmentally sensitive area, is made, the potential E&S risks and impacts of the project will often be significant.

CAO finds that there are good reasons for considering longer-term risks and impacts when IFC makes a decision on the E&S categorization of an early equity mining investment. First, this approach is consistent with the wording of the policy which requires IFC to consider "potential" (as opposed to actual, direct, or immediate) adverse E&S impacts of a project when making a decision on categorization. Second, IFC explains the rationale for its early equity business line on the basis that it is not a speculative or short term investor, but a long term partner for mining projects that have a strong possibility of being developed. This approach suggests that the prospect for development of a mine, with associated E&S risks, is significant. Finally, CAO finds that there may be advantages for IFC and its clients in terms of managing community expectations and concerns if the long term E&S risks attached to early equity mining investments are seen as being fully acknowledged rather than underplayed.

CAO finds that the concerns raised above would most effectively be addressed if IFC provided guidance that the decision as to whether an early equity mining project should be categorized as A or B needs to be determined on a case-by-case basis, taking into account the potential E&S impacts of the project (both immediate and long term), as well as its likelihood of development.

Applying this approach, CAO finds that IFC's Quellaveco investment would properly have been categorized A at the outset, given: (a) the magnitude of the potential impacts of the proposed mine; (b) IFC's view that it had a high likelihood of moving forward to development within a

⁵¹ IFC Comments on CAO Draft Compliance Investigation Report (February 2014).

relatively short period of time; and (c) the potential E&S risks and impacts of the Project in the pre-development phase, in particular potential impacts on Indigenous People.

Further, CAO finds that policy guidance is required in relation to the re-categorization of IFC projects as their risk profile develops. In reaching this finding CAO acknowledges IFC's view that the E&S categorization of committed projects is immaterial in terms of IFC's duties during project supervision. Nevertheless, CAO finds that IFC's categorization plays an important role in communicating project E&S risk to internal and external stakeholders, and as such that re-categorization in response to significant changes in the risk profile of a project may be appropriate.

Rights issues

CAO finds that IFC complied with existing procedures for participating in rights issues in Quellaveco. However, IFC procedures for participating in rights issues as applied to Quellaveco, did not ensure consideration of whether the rights issues would fund "new business activity." To this extent, CAO finds that the procedures were inconsistent with para. 17 of the Sustainability Policy (2006), which implies a requirement to analyze any additional financing in terms of whether it involves "new business activity", and if so to apply the Performance Standards to that investment. In relation to Quellaveco, CAO finds while business activities developed over time, the change was not so significant as to be properly classified as "new business activity." There was thus no breach of the Sustainability Policy in this respect.

More generally, CAO notes that there are significant risks involved in providing additional finance to a project that has inadequate or outdated E&S obligations, or where there is evidence of non-compliance with existing E&S obligations. Given these risks, consistency with IFC's policy commitment to "ensure that the projects it finances are operated in a manner consistent with the requirements of the Performance Standards"⁵² would require IFC's participation in a rights issue to be contingent upon an appropriate review of project E&S risk. IFC's procedures as applied in the processing of rights issues for Quellaveco did not provide for such review. CAO finds this to be inconsistent with IFC's commitment to having clients manage E&S risks in accordance with the Performance Standards as set out in the Sustainability Policy (2006).

To harmonize the procedures for participating in rights issues with the higher level goals of the Sustainability Policy, IFC would need to ensure that appropriate consideration of the current status of a client's E&S obligations and compliance is required before rights issues are processed. Consideration of E&S risk prior to participation in rights issues will be particularly important in relation to: (a) projects that extend over a significant period of time; (b) projects which are operating under superseded E&S requirements; and (c) projects where E&S risk increases over time due to the changing nature of a business activity (such as when an early equity mining investment progresses towards development). While circumstances may exist that justify participation in a rights issue with regard to a project that has no or outdated E&S requirements, or where E&S performance is seriously deficient, following the 2006 Sustainability Policy, CAO would expect that this would be the exception and require specific justification from IFC.

⁵² *Sustainability Policy* (2006) para. 5.

Divestment

IFC's Operational Procedures on Equity Sales require an analysis of whether the investment's purpose has been "substantially fulfilled" prior to divestment. In circumstances where IFC's additionality is framed in terms of E&S issues (as was the case in relation to Quellaveco), this requires an analysis of E&S achievements and future risks. CAO finds no evidence that such analysis informed IFC's decision to divest from Quellaveco. CAO also finds IFC's reporting to the Board was insufficient in this respect.

CAO finds that it would be consistent with both the Operational Procedures on Equity Sales and IFC's broader commitments to E&S sustainability for E&S considerations to be structured into IFC's decision making around divestment. This would allow IFC to determine whether a project has significant outstanding E&S risks, and determine how these should best be managed in the context of a potential divestment. In practice, this might mean a requirement to analyze the current state of E&S obligations and compliance, and take this into account when making the decision to divest. Reference to the current status of E&S compliance, and the approach taken by IFC to mitigating post divestment E&S risk might also be required in the Equity Sale Memorandum.

In conclusion, CAO acknowledges steps taken by IFC E&S staff to supervise emerging risk in relation to the Quellaveco project, despite IFC's investment being made outside the framework of its E&S requirements. At the same time, CAO finds that a more robust framework for considering E&S issues when decisions were made in relation to rights issues and divestment may have put IFC in a better position to respond to the issues raised by the complaint.

Annex 1: Summary of Key Findings

General
The absence of E&S requirements in IFC's Shareholders Agreement for Quellaveco meant that there was a significant gap in terms of the Company's E&S obligations. This made effective E&S supervision difficult.
Nevertheless, IFC supervised the Project with reference to IFC's evolving E&S standards and policies. This represented good practice.
While the Complainants' concerns had not been resolved as at the time of IFC's divestment, CAO finds that IFC's engagement with the Company around E&S issues was generally appropriate to the stage of development of the Project.
Key E&S issues identified by IFC in project supervision were, however, not translated into corrective action plans. Agreeing on corrective action plans would have been of particular relevance in relation to: (a) resettlement activities (which IFC noted were proceeding in advance of the development of studies and plans required by IFC E&S standards); (b) the impact of land acquisition on Indigenous people; (c) issues of stakeholder engagement; and (d) the more technical elements of project design and environmental impact assessment that are discussed in IFC's 2007 and 2010 supervision documentation.
Information presented by IFC to its Board regarding this Project was incomplete, particularly with relation to the E&S standards which applied to the Project and its level of E&S compliance.
E&S Categorization
IFC's Quellaveco investment would properly have been categorized A at the outset given: (a) the magnitude of the potential impacts of the proposed mine; (b) IFC's view that it had a high likelihood of moving forward to development within a relatively short period of time; and (c) the potential E&S risks and impacts of the Project in the pre-development phase, in particular potential impacts on Indigenous People.
The decision as to whether an early equity mining project should be categorized as A or B needs to be determined on a case-by-case basis, taking into account the potential E&S impacts of the Project (both immediate and long term), as well as its likelihood of development.
E&S Considerations around Participation in Rights Issues
IFC complied with existing procedures for participating in rights issues in Quellaveco
IFC's procedures as applied in the processing of rights issues in Quellaveco are inconsistent with IFC's commitment to having clients manage E&S risks in accordance with the Performance Standards as set out in the Sustainability Policy (2006).
IFC's procedures regarding the processing of rights issues are inconsistent with para. 17 of the Sustainability Policy (2006), which implies a requirement to analyze any additional financing in terms of whether it involves "new business activity", and if so to apply the Performance Standards to that investment.
E&S Considerations around Divestment
IFC did not adequately consider whether the investment's purpose has been "substantially fulfilled" in the context of its divestment decision. In circumstances where IFC's additionality is framed in terms of E&S issues (as was the case in relation to Quellaveco), this requires an analysis of E&S achievements and future risks.
IFC's Operational Procedures on Equity Sales do not adequately support IFC's commitments to E&S sustainability in its investments.
It would be consistent with both the Operational Procedures on Equity Sales and IFC's broader commitments to E&S sustainability for E&S considerations to be structured into IFC's decision making around divestment.

Annex 2 – IFC investment in Quellaveco copper project

Project	Type	Approval	Date approved	Amount approved	Disbursement
3823	Initial equity	Board	March 1993	US\$6.22m	Fully disbursed by July 1993
7441	Rights issue	Board	March 1996	US\$5.3m	Fully disbursed by October 1996
10170	Rights issue	Delegated	February 2000	US\$600,000	Fully disbursed by December 2003
10837	Rights issue	Delegated	January 2001	US\$750,000	US\$721,486 disbursed by December 2003
IFC did not participate in rights issues from May 2003. In March 2007 IFC decided to meet previous cash calls to which IFC had not subscribed in order to maintain its stake in the Company. IFC also decided to participate in future rights issues.					
26130	Rights issue	Board	July 2008	US\$12m	Fully disbursed by May 2010
29691	Rights issue	Board	May 2010	US\$18m	US\$15.8m disbursed May 2010
30734	Rights issue	Delegated	March 2011	US\$5m	Fully disbursed by May 2011
31119	Rights issue	Delegated	July 2011	US\$2.1m	Fully disbursed by July 2011
31341	Rights issue	Delegated	September 2011	US\$6m	Fully disbursed by September 2011
31872	Rights issue	Delegated	[Date not known]	US\$3.8m	US\$3.7m disbursed [date not known]

Annex 3 – 2012 Policy – Categorization

40. As part of the review of environmental and social risks and impacts of a proposed investment, IFC uses a process of environmental and social categorization to reflect the magnitude of risks and impacts. The resulting category also specifies IFC's institutional requirements for disclosure in accordance with IFC's Access to Information Policy. These categories are:

Category A: Business activities with potential significant adverse environmental or social risks and/or impacts that are diverse, irreversible, or unprecedented.

Category B: Business activities with potential limited adverse environmental or social risks and/or impacts that are few in number, generally site-specific, largely reversible, and readily addressed through mitigation measures.

Category C: Business activities with minimal or no adverse environmental or social risks and/or impacts.

Category FI: Business activities involving investments in FIs or through delivery mechanisms involving financial intermediation. This category is further divided into:

FI-1: when an FI's existing or proposed portfolio includes, or is expected to include, substantial financial exposure to business activities with potential significant adverse environmental or social risks or impacts that are diverse, irreversible, or unprecedented.

FI-2: when an FI's existing or proposed portfolio is comprised of, or is expected to be comprised of, business activities that have potential limited adverse environmental or social risks or impacts that are few in number, generally site-specific, largely reversible, and readily addressed through mitigation measures; or includes a very limited number of business activities with potential significant adverse environmental or social risks or impacts that are diverse, irreversible, or unprecedented.

FI-3: when an FI's existing or proposed portfolio includes financial exposure to business activities that predominantly have minimal or no adverse environmental or social impacts.

Annex 4: CAO Investigation TOR

[...]

Scope of the Compliance Investigation

The focus of Compliance Investigations is on IFC, and how IFC assured itself of project environmental and social performance at appraisal and during supervision. In the Appraisal report, CAO found that a review of certain aspects of this Project which relate to its nature as an early equity mining investment might better inform the application of policies (or other Compliance Investigation criteria) to future projects.

As set out in CAO's Appraisal report, the Compliance Investigation will focus on the following questions:

- Are IFC's policies and procedures regarding environmental and social categorization of projects, as applied to its investment in Quellaveco, effective to reflect the magnitude of project risks and impacts?
- Are IFC's policies and procedures in relation to rights issues, as applied to its investment in Quellaveco, consistent with IFC's commitment to ensure that the business activities it finances are implemented in accordance with relevant environmental and social standards?
- Do IFC's policies and procedures regarding divestment from projects, as applied to its investment in Quellaveco, ensure appropriate consideration of environmental and social aspects prior to exiting?

The scope of the Compliance Investigation also includes developing an understanding of the immediate and underlying causes for any non-compliance identified by the CAO.

[...] ⁵³

⁵³ Full TOR available on CAO website. http://www.cao-ombudsman.org/cases/case_detail.aspx?id=185