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APPRAISAL REPORT

CAO Appraisal for Audit of IFC

CAO Compliance

C-I-R7-Y09-F105

October 16, 2009

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**Russkiy Mir II Project  
Russian Federation**

**Cases of  
Save Taman/North Caucus Environmental Watch and a Local Stakeholder**

***Summary***

This appraisal report responds to two complaints about the Russkiy Mir II Project (the Project), an IFC investment on the Taman Peninsula of the Russian Federation. The CAO received a first complaint on October 23, 2007 from two NGOs, Save Taman! and North Caucasus Environmental Watch. A second complaint was filed in February 2008 by a local stakeholder raising concerns about pipeline safety. After assessment, the CAO Ombudsman concluded that the parties were not willing to engage in a facilitated solution of the issues raised in the complaints. The first complaint was therefore transferred to CAO Compliance in June 2008, and the second complaint in August 2008 for an appraisal to determine whether the issues in the complaints fulfilled the CAO's criteria to initiate an audit of IFC. These two complaints raised concerns about the impact of the project to the natural and social environment in the region surrounding the Taman Peninsula, health and safety related to the pipeline corridor and IFC's due diligence and environmental categorization in relation to the project.

A third complaint on the Russkiy Mir II Project was filed with the CAO in September 2008 and it is part of an ongoing Ombudsman assessment. This appraisal report relates to the first two complaints.

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



## **Contents**

1. Overview of the CAO Compliance Appraisal Process
2. Background and Concerns that Led to the Appraisal
3. Scope of the Appraisal for an Audit of IFC
4. Policy Provisions Identified as Relevant
5. CAO Findings
6. The CAO Decision

## **About the CAO**

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

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

For more information about the CAO, please visit [www.cao-ombudsman.org](http://www.cao-ombudsman.org)

## 1. Overview of the CAO Compliance Appraisal Process

When the CAO receives a complaint about an IFC or MIGA project, it first refers it to the CAO Ombudsman, which works to respond quickly and effectively to complaints through facilitated settlements, if appropriate. If the CAO Ombudsman concludes that the parties are not willing to reach a facilitated solution, the CAO Vice President has the discretion to request the compliance arm of CAO, CAO Compliance, to appraise the concerns raised in the complaint for a compliance audit of IFC or MIGA. Alternatively, a compliance audit can be initiated by request from the President of the World Bank Group or the senior management of IFC or MIGA.

A CAO Compliance appraisal is a preliminary investigation to determine whether the CAO should proceed to a compliance audit of IFC or MIGA. Through CAO Compliance appraisals, the CAO ensures that compliance audits of IFC or MIGA are initiated only for those cases with substantial concerns regarding social or environmental outcomes.

A compliance audit is concerned with assessing the application of relevant policy provisions and related guidelines and procedures to determine whether IFC and MIGA are in compliance. The primary focus of compliance auditing is on IFC and MIGA, but the role of the sponsor may also be considered.

A compliance audit appraisal, and any audit that ensues, must remain within scope of the original complaint or request. It cannot go beyond the confines of the complaint or request to address other issues. In such cases, the complainant or requestor should consider a new complaint or request.

CAO compliance appraisal will consider how IFC/MIGA assured itself/themselves of compliance with national law, reflecting international legal commitments, along with other audit criteria. The CAO has no authority with respect to judicial processes. The CAO is not an appeals court or a legal enforcement mechanism, nor is the CAO a substitute for international courts systems or court systems in host countries.

The appraisal criteria are set forth in CAO's Operational Guidelines. The criteria are framed as a series of questions to test the value of undertaking a compliance audit of IFC or MIGA. The criteria are as follows:

- Is there evidence (or perceived risk) of adverse social and environmental outcomes that indicates that policy provisions (or other audit criteria) may not have been adhered to?
- Is there evidence of risk of significant adverse social and environmental outcomes that indicates that policy provisions, standards, guidelines, etc., whether or not complied with, have failed to provide an adequate level of protection?
- Is there evidence (or perceived risk) of significant adverse social and environmental outcomes where policy provisions, standards (or other audit criteria) were not thought to be applicable but perhaps should have been applied?



- Is there evidence that the application of some aspect of a policy, standard, guideline or procedure resulted in adverse social and environmental outcomes?
- Can the cause of adverse social and environmental outcomes not be readily identified and corrected through the intervention of the project team without a detailed investigation of the underlying causes or circumstances?
- Could a compliance audit yield information or findings that might better inform the application of policies (or other audit criteria) to future projects?

During appraisal, CAO Compliance holds discussions with the IFC or MIGA project team and other relevant parties to understand the validity of the concerns and to explore whether an audit would be warranted.

After a compliance appraisal has been completed, the CAO can choose only one of two options: to close the case, or to initiate a compliance audit of IFC or MIGA.

The CAO will report and disclose the findings and decision of the CAO compliance appraisal in an appraisal report in order to inform the President of the World Bank Group, the Boards of the World Bank Group, senior management of IFC or MIGA, and the public in writing about its decision.

If the CAO decides to initiate a compliance audit, as a result of the compliance appraisal, the CAO will draw up a terms of reference for the audit in accordance with CAO's operational guidelines.

## 2. Background and Concerns that Led to the Appraisal

1. IFC's project is to develop and build the Taman LPG/Fuel Oil terminal and port in the Black Sea and includes the purchase and expansion of rail maintenance facilities, the acquisition of locomotives and rail cars, a wheel-making / spare-parts manufacturer and other rail-related infrastructure.

2. The first complaint submitted to the CAO raised concerns about the impact of the company's activities to the natural and social environment in the region surrounding the Taman Peninsula. It questioned IFC's environmental categorization of the project as 'B' – rather than 'A', and holds that the environmental review process failed to comply with IFC requirements. The second complaint raises health and safety issues related to the location of the pipeline corridor.

3. IFC's involvement started in 2003, and this is the second investment with the Sponsor. The development is ongoing.

Actions by CAO	
2007	
October 23	CAO receives the first complaint from Save Taman! and North Caucasus Environmental Watch.
2008	
February 26	CAO receives a second complaint from a local stakeholder.
June 16	CAO Ombudsman concludes the assessment of the first complaint and transfers it to CAO Compliance for audit appraisal.
August	CAO Ombudsman concludes the assessment of the second complaint and transfers it to CAO Compliance for audit appraisal.
September 17	CAO receives a third complaint from Save Taman!
2009	
May 22-27	CAO Compliance conducts an appraisal visit to the project site and its surroundings.

### 3. Scope of the Appraisal for an Audit of IFC

4. The complainants have raised specific issues in their complaint regarding:

a. *Incorrect categorization.* IFC's involvement in Russkiy Mir II is classified as environmental category B. The complainants claim the categorization is wrong due to, among other things, irreversible negative environmental and social consequences to the areas in close proximity of the project. They claim the incorrect categorization led to inadequate public consultation and disclosure, and to a simplified review process.

b. *Inadequate public consultation.* The complainants claim there was inadequate public consultation, a failure to invite interested NGOs to the December 17, 2004 public hearing meeting in Taman, and incorrect reporting on the views of community members in the minutes of the meeting.

c. *Violations of IFC's policies and operating standards.* The complainants state that due to incorrect categorization and improper assessment of environmental and social impacts the project violates IFC's policies in the following ways:

- The complainants state that actions taken by Russkiy Mir in construction of the project were in gross violation of Russian legislation by disregarding the requirement of community involvement in the Environmental Impact Assessment (EIA) and not obtaining the proper permits and licenses from state environmental review authorities to commence work on the project.
- The complainants state that the location of the pipeline corridors threatens local farming installations, and therefore violates national legislation.
- The complainants state that the project's EIA does not adequately reflect the environmental and social impact of the project as it misrepresents information in the following ways:
  - Misstating the location or disregarding the existence of several cultural and natural sites in close proximity to the project.
  - Misstating the location or disregarding the existence of residential areas in close proximity to the project.
  - Not taking into account all the factors that are essential for the environmental safety of the project, including the proximity of other high-risk facilities.

d. *Adverse Impacts.* The complainants state that the adverse impacts on the ground will include:

- Irreversible disturbance of marine ecosystems in the Black Sea coastal area (in both Russian and Ukrainian waters).
- Irreversible modification of natural steppe and seaside landscapes.
- Loss of income by rendering health resorts unattractive.
- Increased crime rate and social tensions in the area.
- Threat of environmental disasters due to potential accidents at the project site.
- Destruction of archeological monuments.
- Decreased fishing capacity in the area.
- Decrease in biodiversity and threats to various vulnerable animal and plant species.
- Threats to health and safety related to the location of the gas pipeline corridor.

#### 4. Policy Provisions Identified as Relevant

5. CAO Compliance identified the following provisions as the basis for evaluating the issues raised:

- a. *Incorrect categorization.* IFC's 1998 Environmental and Social Review Procedure states that a proposed project is classified as category 'A' when it likely to have adverse environmental and/or social impacts that are sensitive, diverse, unprecedented or irreversible.
- b. *Inadequate consultation.* An 'A' categorization requires a more diligent approach to consultation than a Category 'B' project.
- c. *Violations of IFC's policies and operating standards* and d. *Adverse Impacts.* The complainants claim that there are several grave factual errors in the EIA that was overseen during IFC's due diligence process, and that IFC did not assure itself that the Project complied with relevant legal requirements and permits. The policy provisions applicable are those relevant to the IFC due diligence process.

#### 5. CAO Findings

6. The appraisal team finds the following:

- a. *Incorrect categorization.* Environmental categorization is determined by scale and extent of environmental and social impacts of a project. As stated in IFC's 1998 Environmental and Social Review Procedure a proposed project is classified as category 'A' when it likely to have adverse environmental and/or social impacts that are sensitive, diverse, unprecedented or irreversible. The complainants state that there are several irreversible project impacts on both environmental and social conditions in the Taman Peninsula. However, the CAO finds that IFC assured itself that there were no unprecedented or irreversible social and environmental impacts by reviewing the facts that:
  - the Russkiy Mir project was located in a site specifically designated for industrial development;
  - several other large-scale industries were being developed in the area;
  - and a certain level of master planning and mitigation plans for the project's impacts have been put in place.

The material difference in categorizing the project as an 'A' rather than a 'B' would be that the Sponsor is required to develop a community consultation plan with an English EIA. As stated also in point b, below, further consultation would not have led to material changes on IFC's due diligence since the complainants state that their intervention would have been to oppose the designation of the project site as appropriate for industrial development, a government decision that pre-dated IFC's due diligence and investment in the project and led to the establishment of the other industrial operations in the area. CAO therefore finds that a category 'B' was appropriate for this project.

- b. *Inadequate consultation.* It is evident from existing due diligence documentation that IFC assured itself that the client had publicly disclosed project documents in accordance with the project's environmental categorization and that the company had held public consultation meetings with community stakeholders. Even in the case that more extensive consultation would have been undertaken, it is the CAO's understanding that this would not have led to material changes in the project as the complainants have stated that their intervention would have been

focused on opposing the designation of the zone as appropriate for industrial development. This designation was a government decision that pre-dated IFC's due diligence and investment in the project and led to the development of the industrial operations in the area. Given the complainants' stated purpose, more extensive community consultation would not have had led to material differences in the project's environmental and social due diligence, or to the level of protection provided by IFC's provisions.

*c. Violations of IFC's policies and operating standards and d. Adverse Impacts.* Based on the existing project documentation, it is evident to the CAO that IFC assured itself that the project ESIA and Environmental and Social Action Plan identified and assessed the relevant social and environmental issues, and the mitigation plans that these issues entailed. IFC's due diligence has specifically taken into consideration plans for oil spills, emergency response, chance finds, community consultation and disclosure, environmental monitoring, compliance with national legislation, and community investment, all of which are raised as issues for concern by the complainants. Given the extent of the documentation, the issues identified and the mitigation plans monitored by the IFC, the CAO finds that the environmental and social due diligence of the project was compliant with IFC's Safeguard Policies and the relevant policy requirements.

The health and safety issues in this case are related to the location of the pipeline corridor, of which there are several in the area including some belonging to other projects. IFC has assured itself that the location of the project's pipeline, particularly in regards to its proximity with local farming installations, is compliant with best international practice and IFC's requirements. During its field visit, CAO Compliance confirmed that the location and conditions of the pipeline were as stated by IFC.

## 6. The CAO Decision

7. The CAO concludes the following:

- a. *Incorrect categorization.* CAO does not find that this issue fulfills the criteria for further investigation in the form of an audit of IFC.
- b. *Inadequate consultation.* CAO does not find that this issue fulfills the criteria for further investigation in the form of an audit of IFC.
- c. *Violations of IFC's policies and operating standards and d. Adverse Impacts.* CAO does not find that these issues fulfill the criteria for further investigation in the form of an audit of IFC.

Based on the above, CAO will close this appraisal with no other further action.