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MONITORING REPORT

CAO Audit of IFC  
CAO Compliance

C-I-R4-Y12-F156  
June 23, 2014

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**Monitoring of IFC's Response**

to CAO's Audit of IFC's Investments in  
Mozal, Mozambique.

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



## **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)

## CAO Compliance Monitoring

As set out in the CAO Operational Guidelines, CAO Compliance keeps a compliance audit open and monitors the situation until actions taken by IFC/MIGA assure CAO that IFC/MIGA is addressing any non-compliance found. On completion of its monitoring function CAO closes its compliance process.

### Background

In April 2013, CAO released an audit of IFC's investment in Mozal, Mozambique.

Mozal, located 20 kilometres west of Maputo, is an aluminum smelter. At the time the audit was prepared, IFC had two active investments in the project: the first, approved in 1997, supported the construction and operation of the smelter, and the second, approved in 2001, supported doubling its production capacity. BHP Billiton, a publicly traded international mining and metals group, is the primary sponsor of Mozal.

CAO's audit responded to a complaint from communities living near the smelter. The complaint raised concerns regarding a decision to run the smelter while bypassing Fume Treatment Centers (FTCs), which clean emissions from the plant's carbon anode bake house. The bypass operation was required because corrosion problems in the FTCs. The smelter ran bypassing the FTCs for a period of 134 days from November 2010 to March 2011 during which time plant's emission levels were increased.

### CAO Audit Findings

CAO found that the need for the FTC bypass had become critical before IFC became aware of it in late 2009. Preparations for the bypass thus occurred in a compressed schedule. Though ambient air quality remained mostly within relevant limits during the FTC bypass, the compressed schedule for preparation for the bypass operation impacted the time that was available for community consultations and health impact studies.

CAO also found that the risk of failure of the FTCs could reasonably have been anticipated before the need for the bypass was communicated to IFC. In a context where IFC was aware of an earlier corrosion incident requiring bypass of the FTCs in 2001, CAO found that it would have been appropriate for IFC to have requested that Mozal assess, monitor and report regularly on its approach to the management of risks associated with a possible future failure of the FTCs. Had this been done, IFC could have been aware of the likely need for an FTC bypass operation as early as 2007.

Analyzing the reasons why engagement with these risks did not feature as part of E&S supervision, CAO found that both IFC and Mozal assumed that the risk of failure of the FTCs was outside the scope of their reporting relationship so long as agreed FTC uptime and point emission targets were being met.

This, CAO found, represented an unduly narrow interpretation of the Sustainability Framework; and one that could be clarified with a view to enhancing IFC's approach to the management of environmental and social risk in its investments.

### **IFC's Response to the Audit**

In its response to the CAO audit, IFC states that it believes that staff took reasonable and timely actions consistent with policy and procedures in relation to the issues raised by the complaint. IFC also states that engineering aspects such as those raised by the CAO audit are outside the scope of IFC's environment and social supervision practices and procedures. In this context, IFC explained that it was satisfied that its client, BHP Billiton, had a well-qualified and experienced team which was managing the corrosion risks to the FTCs.

IFC's response acknowledges, however, that CAO's report raises an important question about the adequacy of annual reporting when an important issue is identified (particularly in a mature portfolio investment). As such IFC undertakes to give consideration to changes in reporting requirements to deal with circumstances such as this.

In subsequent communications with CAO IFC has pointed to the addition of the following language in the Environmental and Social Review Procedure (ESRP) as responding to this issue:

**2.4 Special reporting requirements:** In those circumstances when specific aspects of the project rise significant E&S concerns IFC may request supplemental project information in addition to the AMR and on a quarterly or even monthly basis depending on the nature of the issue and its potential E&S consequences. These special reports will allow IFC to monitor more closely those specific aspects. In these cases additional supervision site visits may be required too (*ESRP 6: 04/15/2013*).

### **Developments Subsequent to the Audit at Mozal**

In October 2012, Mozal submitted an Annual Monitoring (AMR) report to IFC covering the period July 2011 to June 2012. IFC's review of the AMR identified no major issues and rates the project's E&S performance satisfactory.

In April 2013 Mozal informed IFC of further damage to one of the FTCs caused by fire. As a result Mozal informed IFC that it would be necessary to operate the FTC unit on bypass mode for a total of 5 weeks. At this point Mozal reported that it had sought government approval to operate on FTC bypass and that it was engaging with stakeholders around the need for the shutdown. Mozal also reported that it had engaged an external consultancy firm to monitor ambient air quality in the area of the plant to ensure that the impact on the environment was understood. Finally, Mozal reported that it would conduct a full investigation in order to understand the root causes of the problem with the FTC.

In May 2013 IFC E&S staff conducted a site supervision visit to Mozal which included a visit to the FTCs and selected air monitoring sites. IFC's back to office report (BTOR) from the supervision visit articulates Mozal's analysis of the causes of the damage to the FTCs. The BTOR outlines mitigation measures proposed by Mozal to prevent reoccurrence of the problem and relates that no ambient air parameters were exceeded during the fire event. The BTOR also reports that Mozal communicated with its stakeholders including employees, the government, its lenders and stakeholders in the surrounding industrial zone.

In October 2013, Mozal prepaid the remainder of its loan to IFC.

### **Conclusion**

IFC has expressed its disagreement with the central finding of CAO's audit of its investment in Mozal, namely that IFC's approach to project supervision was insufficiently responsive to changes in project E&S risk profile. Rather IFC maintains that it relied appropriately on its client's expertise in relation to engineering issues that are outside the scope of IFC's environment and social supervision duties.

The 2013 addition to the ESRP cited above provides that IFC may request supplemental project information if specific aspects of a project raise significant E&S concerns. This provision does not address the issues raised by the CAO audit of IFC's investment in Mozal either in terms of: (a) IFC's approach to supervision of changes in project E&S risk or, (b) client reporting requirements in relation to such changes.

CAO discussed additional measures with IFC such as the revision of client E&S reporting formats and staff training that might address the findings of the Mozal audit but IFC did not take these up.

CAO thus rates IFC's response to this audit Unsatisfactory.

Nevertheless, as IFC's investment in Mozal is no longer active, and as the CAO audit did not identify project level compliance issues which require remedy, CAO has decided to close this compliance process.