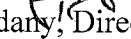


THE WORLD BANK/IFC/M.I.G.A.

OFFICE MEMORANDUM

DATE: October 14, 2005

TO: Meg Taylor, Vice President, CAO

FROM: Rashad Kaldany,  Director, COCDR

EXTENSION: 36787

SUBJECT: CAO Assessment Report: Complaint Regarding Marlin Mining Project in Guatemala

1. **Introduction.** IFC has reviewed the CAO Assessment Report (the "Report") dated September 7, 2005, regarding the Marlin project (the "Project") in the Department of San Marcos, Guatemala. IFC agrees with the CAO's recommendations as summarized on page *iv* of the Report, and we intend to continue working with stakeholders to implement the CAO's recommendations. More generally, IFC welcomes the input and insights of the CAO since we share the common objective of enhancing the social and environmental outcomes of the Project. At this point the most important matter is to move the Project forward in a way that is peaceful and respectful of all stakeholders and that ensures that the benefits of the Project result in sustainable development.

2. **CAO Recommendations Specific to the Marlin Mining Project.** Most of the CAO's recommendations specific to the Project are already being implemented. For example, in regard to the CAO's first recommendation to "Promote a comprehensive and participatory plan for the public monitoring of environmental performance of the project", a monitoring committee has already been formally established and consists of representatives of: (a) the six villages closest to the mine in San Miguel Ixtahuacán and Sipacapa (these representatives were selected by traditional means), (b) the Catholic and Evangelical churches, (c) the University of San Carlos and the University del Valle (which will provide technical input and training), (d) the mayor of San Miguel Ixtahuacán (discussions are underway with the mayor of Sipacapa), and (e) a facilitator selected by the six villages, namely Mr. Victor Ayala of Fundacion ProPaz which is an NGO established by the Organization of American States. It is important that the work of the committee be based on sound science and facts, and care must be taken to ensure that politics is not permitted into the process. The success of this committee will go a long way to reassure the people of both municipalities, and the work of the committee should be supported by all.

In regard to establishing "a framework for an on-going dialogue and consultations", the government is taking a number of positive actions to build consensus and address the issues related to the future of mining in Guatemala. These include: (i) the agreement signed on August 23, 2005, by the High Level Commission on Mining that outlines a way forward for responsible metallic and other mining in Guatemala. This agreement was signed by a diverse group of national organizations, including, among others, the MEM, ASOREMA (a coalition of about 15 environmental NGOs), Colectivo MadreSelva (one the CAO complainants) and the Catholic Church (Bishop Ramazzini). The agreement suggests guidelines on issues related to mining areas, consultations (ILO 169),

socio-economic development, protection of the environment, royalties and taxes, license applications and administrative procedures. This should be viewed as a positive step along the path of dialogue and consensus building about mining; (ii) development of the government's "Plan San Marcos" which has been called a "Marshall Plan for San Marcos". During President Berger's recent visit to San Marcos Department (the poorest in Guatemala), the request of local communities for increased investment in infrastructure was agreed, and Montana Exploradora agreed to fund \$5 million for a road that is not needed for the mine but which will enhance economic development of the region; (iii) a 25-member delegation led by Bishop Ramazzini recently visited the mine. This permitted a first-hand exchange of views and a forum for questions to be asked of the company on a wide range of social, environmental and economic issues. The feedback was that this was a positive meeting, although certainly many disagreements remain; and (iv) the continued upgrading of government's capacity to regulate mining.

3. General Recommendations Not Specific to the Marlin Project. In Section 3.3 the CAO has outlined a number of general recommendations for IFC relating to its procedures and project assessment. A draft of IFC's revised Environment and Social Review Procedures is now available, and we welcome the CAO's comments on this document. It is our intention to more systematically document the decision process that IFC staff follows throughout the project review, and we hope that this will help alleviate CAO concerns in this regard. As noted by the CAO, the draft IFC Policy and Performance Standards on Environment and Social Sustainability also addresses some of the general concerns and recommendations made in the report. The Guidance Notes to the Performance Standards will provide further help in this regard, and IFC is currently prioritizing the need for further good practice notes to assist clients. The CAO's specific observations and recommendations regarding the need for such guidance will be taken into account as we prepare this guidance material.

4. Issues in the CAO Report Requiring Further Clarification. In the spirit of ensuring that facts are correct, we wish to raise a number of issues from the CAO's Report that we believe need clarification. We regret that a number of important comments that IFC made to the CAO's confidential draft report of July 2005 were not taken into consideration in the CAO's final Report. In addition, the Report contains some ambiguities and incorrect dates and facts. In this memo we will limit our comments to the most important of these issues, but we would welcome the opportunity to meet with you and your staff to review other, but less critical, errata.

4.1 Environmental Impact. IFC welcomes the conclusion of the CAO that with regard to environmental risks "the people of Sipacapa are not likely to be impacted significantly by the project." The CAO findings uphold the original IFC assessment of the Project. However, the CAO Report does give the wrong impression on this matter. This is because the main body of the CAO Report refers only to the lack of impacts in Sipacapa, presumably since the complainants, other than Colectivo MadreSelva, are only from Sipacapa. The complaint itself is concerned about the impact on the entire area. The confusing fact is that the main body of the Report ignores the important annexed conclusion of the CAO's independent technical consultant that there will be no adverse environmental impact by the Project in the entire area, i.e., either in Sipacapa or in San Miguel

Ixtahuacán. It would have been more accurate and helpful for the CAO to state the fact that the Project is not likely to have a significant environmental impact or have risks that are inadequately mitigated in either Sipacapa or San Miguel Ixtahuacán.

4.2. Anti-Mining Campaign. IFC agrees with the findings of the CAO that the project has become a focal point for an aggressive and at times factually unfounded campaign which has led to heightened fear and tension amongst some local people. When people in Sipacapa were falsely told that the Project would have adverse, unmitigated environmental impacts, it is easy to understand how some could come to oppose the Project and say that they were not informed or consulted about such purported negative impacts.

4.3 Security. The CAO opines that: “IFC failed to make any consideration of potential for local-level conflict in its appraisal or advice to the Sponsor.” We believe that this statement is incorrect, and that the Report mischaracterizes the situation with regard to security concerns.

During appraisal in October 2003, IFC staff did discuss security issues with Montana. IFC discussed with the company the security of the mine site and whether it was needed to fence the property, and if the unarmed security guards at the site entrance provided sufficient protection. The company also indicated that care had to be taken when going into certain villages and areas in the region because of the risk to personal security. The company’s view at the time was that despite the violence during the civil war, it was a peaceful area, and the mine’s remote location on top of a mountain led them to the conclusion that no particular security measures were required. They indicated that they preferred to avoid the risk of the perception of a threat (and the additional cost) by not having armed security personnel. The company did indicate to IFC that common sense precautions had to be observed such as not traveling alone, not going into certain villages without an appropriate escort and introductions from local people, etc. Unfortunately, these issues were not recorded in IFC’s back-to-office memos, just as many other issues that are discussed during an appraisal are for practical reasons not always written down. This is something we will need to be more diligent about in the future.

The company did not hire armed security guards until mid-2004 when threats against mine workers began. Until then, the Project was operating in peace with no signs of conflict with neighboring communities.

One of the violent incidents mentioned in the Report (the blockade in Los Encuentros, about 120 kilometers from the Marlin mine) was unrelated to security under the control of the company, and the other incident was a result of a domestic argument unrelated to the Project. The CAO Report should have clarified these facts. The incidents were tragic and regrettable, but we believe that shortcomings in the Company’s security policies were not the reason these incidents occurred.

It should be pointed out that Montana has made changes to its security procedures over the last few months. Of significant importance, Glamis Gold Ltd. has made the commitment to incorporate the US-UK Voluntary Principles on Security and Human Rights in all of its operations. In sum, progress is being made on the important issue of security.

4.4 Disclosure and Consultation by Montana and the Government. IFC welcomes the findings of the CAO that amongst other matters: (i) "...the company has interacted extensively with local communities...", (ii) "...individual land transactions were successful", (iii) "...local leaders in both San Miguel and Sipacapa signed documents submitted to government regulatory agencies expressing support for the project", and (iv) "... the company responded to public survey findings of the ESIA process by changing some of its design plans for the project."

When IFC appraised the Project we found that the company handled the disclosure and consultation process in a responsible and culturally appropriate manner under the supervision of the government. However, the CAO Report opines that there was an: "... absence of meaningful consideration of the cultural and linguistic distinctiveness and minority status of Sipacapa...". We do not agree with this statement. The company chose to employ Sipacapense, as well as Mam, indigenous peoples to work in their Community Relations Group and these staff played key roles in the consultation process and in the identification of projects to address immediate and long-term needs of local communities—roads, water, support to local schools, health services and permanent jobs. The CAO presents no evidence of culturally inappropriate behavior on the part of Montana. In fact, we have observed and been favorably impressed by the respect with which the company treats the local communities.

The CAO Report also questions how the IFC determined that consultations with the affected communities were "meaningful". IFC reached this conclusion on the basis of direct observations during appraisal, the review of the Public Consultation and Disclosure Plan prepared for IFC, and the evidence presented in other Project documentation, such as the Indigenous Peoples Plan and the Land Acquisition Procedures.

4.5 Thoroughness of IFC's Appraisal and IFC's Procedures. The CAO opines that the process by which IFC judged the adequacy of the environmental and social impact assessment was not clear and the timing of completion of some key documents has not always been sufficient to allow informed public scrutiny. IFC believes that there is a lack of understanding on the part of the CAO with regard to IFC's environmental and social review procedures. Environmental and social specialists exercise their professional judgment when approving EIAs and supplemental information requested by IFC. The Environmental and Social Department does not produce a special document justifying this decision. This is

true for all projects, not just for the Marlin project. The practice at IFC is not to publish EIAs and related documents in the World Bank InfoShop until we are comfortable that these documents address all important impacts and mitigation measures.

We disagree with the CAO Report that "... the IFC appraisal process ... was not fully recorded." This criticism is unrelated to the complaint and unsubstantiated by the CAO. While there is always room for improvement in any project, IFC's procedures were followed, documented and subjected to IFC's multiple-level approval process as the following partial list indicates:

- IFC's initial written assessment in September 2003 of the ESIA and other Project documentation identifying applicable policies and guidelines, and potential Project issues.
- Text provided by IFC's Environment and Social Department ("CES") for the PDS Early Review. Issues mentioned include some that the CAO erroneously opines have been overlooked by IFC, such as in-migration.
- Minutes of the CES Peer Review Meeting on October 22, 2003. The Peer Review Meeting is a part of IFC's processing procedures wherein all colleagues from the CES department, as well as those from other departments, are invited to meet to critique and offer suggestions in regard to the social and environmental aspects of IFC's projects. Subjects discussed in regard to the Marlin project included: application of various Safeguard Policies to the Project; use of cyanide; independent review of the tailings dam; mine closure; and the implications for the indigenous people in the area.
- Back-to-Office Report dated October 28, 2003, of Mauricio Athie and José Zevallos, IFC environmental and social specialists. The section of this report on the Environmental Impact Assessment states the following:
 - To comply with IFC requirements the sponsor would need to provide additional documentation including the following:
 - An Environmental Action Plan. The EAP will include measures to address induced migration to the area and a commitment to undertake an independent review of the proposed tailings facility.
 - Safety of Dams Report. This will be a large dam requiring an independent panel review. The terms of reference for the independent reviewer must include consideration to: the water balance; flash flood type situations; continuing monitoring role throughout design, construction and mine life; construction method appropriate for a seismic zone; stability after closure, particularly with regard to drainage and earthquake issues.
 - Hazardous Materials Management Plan and an Emergency Preparedness and Response Plan according to IFC guidelines.
 - Mine Closure Plan. Short mine life (11 years) will need closure plan with commitment to funding at any point in mine life.

- Indigenous Peoples Development Plan to ensure that indigenous peoples in the area share in the benefits of the Project.
- Land Acquisition Procedures.
- Public Consultation and Disclosure Plan.”

- IFC’s comments regarding ESIA documentation (e-mail from the IFC Investment Officer to Glamis Gold dated November 14, 2003). The e-mail requests the documents listed in the previous bullet point and includes comments/guidance on the Land Acquisition Procedures and Indigenous Peoples Development Plan.

- Minutes of IFC’s Corporate Investment Committee (“CIC”) dated November 24, 2003. The CIC is IFC management’s highest level review committee, and the minutes of this meeting record the discussion of the Project’s potential environmental and social impacts, including the tailings dam, the use of cyanide, the hazardous material assessment and management plan, land acquisition, protection of cultural property and water use.

- Environmental and Social Considerations in the Investment Review Memorandum. This document discusses key environmental issues and states that the company “adequately addressed these issues in its Environmental Impact Assessment (EIA) and supporting documentation”. This document also discusses Montana’s capacity to comply with IFC requirements and some key compliance measures, such as the Indigenous Peoples Development Plan.

- Minutes of the Investment Review Meeting dated February 27, 2004 (this is the meeting attended by all relevant IFC departments/specialists (including Environment and Social, Legal, Insurance, Credit, engineering) where all issues are debated and a decision made whether or not to proceed with final negotiations with the sponsor. The minutes show the degree of importance IFC management and Project team placed on ensuring that the Project would be implemented according to the highest environmental and social standards and in full compliance with IFC policies. Key environmental issues were discussed, as well as resettlement and land acquisition, indigenous peoples in the Project area, consultations, etc.

- Documents developed by Montana in order to comply with IFC requirements, including the Public Consultation and Disclosure Plan, the Land Acquisition Procedures and the Indigenous Peoples Plan. IFC staff provided advice and feedback on a regular basis during the preparation of these documents.

- Environmental and Social Clearance Memorandum dated April 13, 2004, refers to the environmental and social reference documents for the loan agreement, the applicable policies and guidelines, clauses and conditions to be included in the loan agreement, and the Project’s reporting requirements.

- Environmental and Social Section of the Board Report. This section describes key social and environmental issues and states that the Company “adequately

addressed these issues in its Environmental Impact Assessment (EIA) and supporting documentation” and has also “demonstrated adequate capacity to comply with IFC requirements.”

- Guidance for the preparation of Marlin’s Annual Environmental and Social Monitoring Report (sent in an e-mail dated June 21, 2004, from the Investment Officer to Glamis Gold).
- Memorandum on Marlin Social and Community Monitoring dated October 17, 2004. This Memorandum (from George Blankenship, Montana’s social consultant, to J. Zevallos) outlines the socioeconomic and community monitoring tasks for the Marlin project.
- Environmental Audit and Review of the Marlin Project (prepared by Dorey & Associates Consulting and reviewed by Patricia Acker Consulting, L.L.C, and dated January 2005. This Audit contributed to the timely completion of the Environmental Management Plans required for operations. This Audit was required by IFC and will be carried out annually.
- Three reports issued as part of the Independent Review of the Tailings Storage Facility required by IFC.
- Marlin’s Environmental and Social Annual Monitoring Report (AMR). This report was developed with IFC guidance. IFC requests AMRs in order to evaluate compliance of our projects with IFC policies and guidelines.

We would note one further misleading finding of the CAO Report. The CAO states (Section 2.2.1.5) that the Environmental Audit and the Tailings Dam Review Report both “note that development and/or implementation of some important management measures and plans during construction was [sic] behind schedule.” This is inaccurate. All plans have been completed in a timely manner as required by IFC. The only issue that the Environmental Audit found was that some inexpensive erosion control structures had not been constructed as planned, but the impact was minor. In any case these structures have since been built.

Lastly, we believe that it would have been helpful if the CAO had mentioned what IFC has done to improve the Project—a number of IFC interventions, such as the requirement for an Independent Environmental Audit and the establishment of the Tailings Storage Facility Review Board, were not in fact required by IFC procedures, but we thought they made sense given the business context.

4.6 Government Regulations and Capacity to Regulate. With regard to the central government’s capacity to regulate the mining industry, IFC and the World Bank have been clear from the beginning that improvements are needed. This is in part because limited resources have been available for upgrading regulatory capacity since so little mining has occurred in Guatemala. However, an important role of the World Bank

Group is to work with governments to help develop that capacity as the mining sector develops. To this end the World Bank has been providing input to government on the mining regulatory framework, and the process of implementing changes is being developed. The High Level Commission agreement dated August 23, 2005, is part of the process of getting consensus on the desired regulatory environment.

Despite limited resources, the government does have competent professionals supervising the Marlin project, and its capacity to regulate continues to be upgraded as is of course needed. For example: (i) the MARN has recently hired two new inspectors for San Marcos department, and they have received new equipment, computers, etc.; (ii) the MEM has its own mining control department with geologists, engineers, and environmental specialists. They are part of the MEM inspection team that has been at the Marlin site for about 5 days at least every month; and (iii) the MEM will have its own lab at the Marlin site for environmental monitoring. They will man it and will also have senior year university chemistry majors work at the lab for 6 months each as part of their graduation requirements which will of course over time help develop additional knowledge and regulatory capacity in the country.

With regard to the legal regulatory framework, the CAO states that: “The absence of clear government regulations has resulted in uncertainty for both the investor as well as local people about the extent to which they should have been informed and consulted about mining.” It should be pointed out that ILO Convention 169 is itself ambiguous and few of the 17 countries that have ratified the Convention have actually put in place implementing regulations. This may be testimony to the practical difficulty of doing so, particularly in a country like Guatemala where the majority of the population is indigenous. While IFC recognizes that no clear guidance for the implementation of ILO Convention 169 exists in Guatemala, during appraisal IFC assured itself that:

- a) Exploration activities took place on privately owned land with the consent of affected landowners and the knowledge of municipal authorities. The landowners gave permission to the geologists and other Project staff to enter their property and do their work.
- b) Our understanding is that the intent of the ILO was satisfied in regard to exploration given the nature of the affected population.
- c) All land acquired by Montana Exploradora was obtained with the consent of the individual landowners through a process of willing seller/willing buyer interactions.
- d) The relocation of families who decided to sell their lands was done according to international best practice and adhering to the IFC safeguard policy OP 4.12 and in compliance with Article 15 of ILO Convention 169 which provides for consultation with indigenous peoples and their participation in the benefits of exploitation in those instances where the state controls the mineral resources.
- e) Montana behaved respectfully vis-à-vis the affected communities. As a result of consultations that began during the exploration phase,

Montana funded a number of social projects in San Miguel Ixtahuacán and Sipacapa that were requested by those communities.

In conclusion, while we have described once again a number of inaccuracies in the CAO Report, we feel that the recommendations are sound and look forward to discussing these with you and your staff in the spirit of moving ahead in a constructive manner.

cc: Messrs./Mmes. A. Jabre, F. Khambata, R. Kyte, A. Mehta, K. Lupberger, K. Harry, W. Bulmer, M. Swetye, J. Zevallos, M. Athie, F. Pittaluga, C. Armstrong, H. von Hindenburg, T. Bruington, A. Inamdar, N. Robertson