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## **Terms of Reference for Compliance Investigation of IFC’s Environmental and Social Performance in relation to Exposure to Six Financial Institutions in Cambodia (Acleda, Amret, Hattha Bank, Prasac, LOLC, and Sathapana)**

*IFC Project Numbers: #21856, #27827, #31467, #34748, #38609, #39167, #41294, #42480, #44211, #44231, #44742, #44882, #45535*

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### **About CAO**

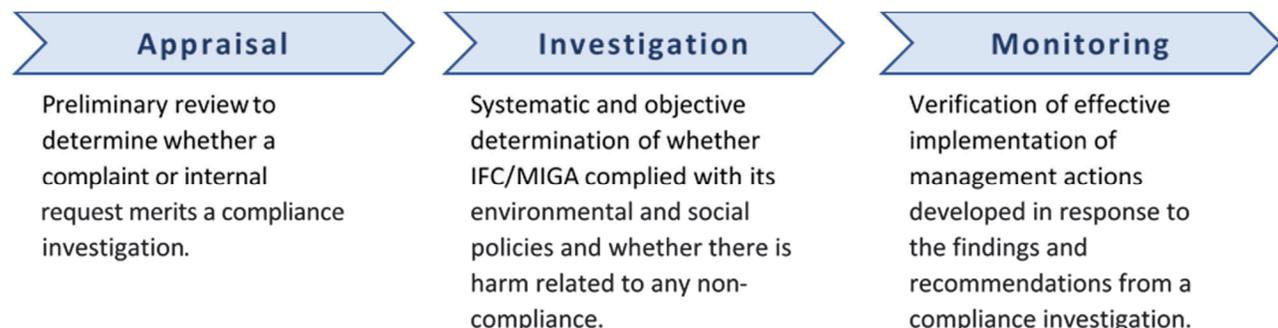
The Office of the Compliance Advisor Ombudsman (CAO) is the independent accountability mechanism of the International Finance Corporation (IFC) and Multilateral Investment Guarantee Agency (MIGA), members of the World Bank Group. We work to facilitate the resolution of complaints from people affected by IFC and MIGA projects in a fair, objective, and constructive manner, enhance environmental and social project outcomes, and foster public accountability and learning at IFC and MIGA.

CAO is an independent office that reports directly to the IFC and MIGA Boards of Executive Directors. For more information, see [www.cao-ombudsman.org](http://www.cao-ombudsman.org).

### **About the Compliance Function**

CAO’s compliance function reviews IFC and MIGA compliance with environmental and social policies, assesses related harm, and recommends remedial actions where appropriate.

CAO’s compliance function follows a three-step approach:



## Context and Investment

Over-indebtedness of poor and vulnerable populations is a growing concern in Cambodia.<sup>127</sup> The World Bank, IFC, and different UN agencies have all raised concerns about the increasing over-indebtedness of Cambodian households, which together with a weak consumer protection framework, has adverse social repercussions and affects many Cambodians' standard of living.<sup>128</sup>

The WBG has provided extensive support to Cambodia's financial sector through technical assistance and direct investments, particularly for the provision of microfinance and the development of financial infrastructure. IFC has made significant investments in several microfinance institutions. Related to this case, IFC has direct investments in Acleda Amret and Hattha Bank, as well as indirect financial exposure to Prasac, LOLC, and Sathapana through investments in the Microfinance Enhancement Facility (MEF), the Microfinance Initiative for Asia Debt Fund (MIFA), North Haven Thai (a private equity company), and Advans S.A. (Amret's parent company). In total, this case involves 13 IFC projects, that support lending programs for micro, small, and medium enterprises (MSME) which were active at the time the complaint was filed with CAO, and which link IFC to these six financial institutions in Cambodia.

## The complaint

In February 2022, CAO received the complaint in relation to the lending and collection practices of Acleda, Amret, Hattha Bank, LOLC, Prasac, and Sathapana Bank in Cambodia. The complainants argue that IFC has repeatedly failed to conduct adequate environmental and social (E&S) due diligence and supervision on its clients who are microfinance providers. They allege the clients' Environmental and Social Management Systems (ESMS) are "clearly inadequate to address the predatory and deceptive loan practices, irresponsible lending [...], and coercion and threats from loan officers" that are common practice in Cambodia.

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<sup>127</sup> See, among others, IFC, Promoting Financial Consumer Protections in Cambodia, 2015, pp. 29–33. Available at <https://bit.ly/3VCU817>; World Bank Group, Cambodia Policy Note on Microfinance and Household Welfare, 2019, p.11. Available at <https://bit.ly/3NITywL>; MIMOSA Report on Cambodia, March 2020, p. 7-8.

<sup>128</sup> Report of the UN Secretary-General to the Human Rights Council, Annual Report of OHCHR, Role and achievements of the Office of the United Nations High Commissioner for Human Rights in assisting the Government and people of Cambodia in the promotion and protection of human rights, 17 August 2022, A/HRC/51/63, para. 42; Report of the UN Secretary-General to the Human Rights Council, Role and achievements of the Office of the United Nations High Commissioner for Human Rights in assisting the Government and people of Cambodia in the promotion and protection of human rights, 16 September 2021, A/HRC/48/49, para. 40; UN Independent Expert Report on Private Debt and Human Rights, Report of the Independent Expert on the effects of foreign debt and other related international financial obligations of States on the full enjoyment of human rights, particularly economic, social and cultural rights, (2020), A/HRC/43/45 at p.1 and para. 32–34; Committee on Economic, Social and Cultural Rights, Concluding observations on the second periodic report of Cambodia, 27 March 2023 E/C.12/KHM/CO/2, paras. 38 and 39(b).

Specifically, the complainants allege that they have lost their land and livelihoods because microfinance lenders routinely request them to put up their land as collateral for the loans to be approved, including indigenous communal land, and then force them into premature sales of the land for collection. Moreover, to repay increasing debts, they have also sold other sources of income, such as tools, reduced their food intake, taken their children out of school, and been forced to migrate for work. The complainants state that IFC was aware of publicly available information regarding widespread social harms and inadequate consumer protections in Cambodia's microfinance sector but continued to approve additional financing in the sector without additional requirements. They argue that IFC is not properly supervising the business activities of its microfinance clients on the grounds that microfinance lenders are not required to screen their lending activities for E&S risks and resulting harms to borrowers. They consider this particularly significant since microfinance borrowers are likely to be part of vulnerable populations and thus require more protection and monitoring to ensure that IFC projects do not have harmful social impacts.

The complainants have also expressed a fear of reprisals for speaking out against the microfinance industry and have asked CAO to keep their identities confidential.

### **Investigation Terms of Reference**<sup>129</sup>

Where, as in the present case, the CAO appraisal process results in a decision to investigate, CAO's appraisal report includes terms of reference for the compliance investigation, outlining:

- a. *The objectives and scope of the investigation;*
- b. *Any limitations on the scope of the investigation that may be appropriate, considering, among others, issues closed at the appraisal stage, the presence of concurrent judicial proceedings, or an IFC/MIGA Exit;*
- c. *The approach and method of investigation and specific consultant qualifications; and*
- d. *A schedule for the investigation tasks, timeframe, and reporting requirements. This schedule will include deadlines for the submission of information by IFC/MIGA to inform the compliance investigation process.*<sup>130</sup>

### **Investigation Objective and Scope**

As established in the Compliance Appraisal Report, and as related to the complaint, CAO will conduct a compliance investigation of IFC's investments in Acleda, Amret, Hattha Bank, Advans, North Haven Thai, MEF, and MIFA, and indirect investments in Prasac, LOLC, and Sathapana, through MEF and MIFA. The investigation will determine whether IFC complied with its E&S Policies relevant to the investments and whether there is harm related to any IFC non-compliance. In determining whether IFC has complied with its E&S Policies, CAO will include,

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<sup>129</sup> Following para. 119 of the CAO Policy, CAO consulted with IFC in preparing these TOR.

<sup>130</sup> CAO Policy, para. 118.

where appropriate, an assessment of whether IFC deviated in a material way from relevant directives and procedures.

Relevant to the issues raised in the complaint, the objective of the investigation is to determine:

1. Whether IFC has complied with its E&S Policies, including:
  - a. Whether IFC conducted a pre-investment E&S review of its investments in Acleda, Amret, Hattha Bank, Advans, North Haven Thai, MEF, and MIFA as required by the Sustainability Policy that was commensurate to the risks and impacts of these investments on the MSME borrowers (sub-clients in these investments); and
  - b. Whether IFC put in place contractual provisions requiring its clients named above to meet Cambodian national law, the IFC Exclusion List and the IFC Performance Standards, as relevant to each investment, regarding risks and impacts on the MSME borrowers; and
  - c. Whether IFC has supervised its investments in Acleda, Amret, Hattha Bank, Advans, North Haven Thai, MEF, and MIFA to ensure they comply with the requirements of Sustainability Policy, the Performance Standards, the IFC Exclusion List, and national law, as relevant to each investment, regarding risks and impacts on the MSME borrowers.
2. Whether the harms and potential harms raised by the complainants are related to any IFC non-compliance.<sup>131</sup>

In considering findings regarding harm and whether any harm is related to IFC non-compliance, CAO will assess IFC's review and supervision of its E&S requirements under the Sustainability Policy and the Access to Information Policy. CAO will consider project E&S performance including in relation to the application of the Performance Standard 1 (Assessment and Management of Environmental and Social Risks and Impacts), Performance Standard 7 (Indigenous Peoples), and the Exclusion List as relevant to the issues raised in the complaint.

## **Methodological Approach**

CAO will base the compliance investigation on interviews, statements, reports, correspondence, CAO observations of activities and conditions, and other sources that CAO deems relevant.<sup>132</sup> The compliance investigation process and compliance investigation report will include:

- a. *The investigation findings with respect to compliance, non-compliance, and any related Harm.*
- b. *Context, evidence, and reasoning to support CAO's findings and conclusions regarding the underlying causes of any non-compliance identified.*

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<sup>131</sup> CAO Policy, paras. 112–114.

<sup>132</sup> CAO Policy, paras. 115 and 117.

- c. *Recommendations for IFC/MIGA to consider in the development of a Management Action Plan (MAP) relating to the remediation of project- or sub-project-level non-compliance and related Harm, and/or steps needed to prevent future non-compliance, as relevant in the circumstances. In case of a project where the IFC/MIGA Exit has occurred, recommendations will take into account the implications of such an IFC/MIGA Exit.*<sup>133</sup>

Sufficient, relevant evidence is required to afford a reasonable basis for CAO's compliance findings and conclusions. CAO will assess whether there is evidence that IFC applied relevant E&S requirements considering the sources of information available at the time the decisions were made and will not make findings and conclusions with the benefit of hindsight.<sup>134</sup>

## **External Expert(s)**

Following established practice, CAO will engage one or more external experts for this investigation, and considers the following qualifications as necessary:

- Significant expertise and experience in microfinance investments, responsible finance, and financial consumer protection standards;
- Significant expertise in land rights and Indigenous Peoples land issues in Cambodia;
- Significant expertise in socio-economic assessments;
- Knowledge of ethnic groups and indigenous peoples in Cambodia;
- Knowledge of the regulatory framework, practices, and procedures of microfinance institutions in Cambodia;
- Knowledge of IFC's E&S policies, standards, and procedures, particularly the Sustainability Policy, Performance Standard 1 (Assessment and Management of Environmental and Social Risks and Impacts), Performance Standard 7 (Indigenous Peoples), the IFC Exclusion List, and the Access to Information Policy;
- Experience and knowledge relevant to conducting compliance investigations;
- Experience in managing, addressing and considering risks of threats and reprisals to complainants.
- Demonstrated ability to analyze policies and practices and develop proposals for reform in complex institutional contexts; and
- Fluency in Khmer and English.

## **Field Visit**

Field visits to complainants' communities are anticipated during the compliance investigation, as well as to the offices and/or branches of Aceda, Amret, Hattha Bank, LOLC, Prasac, and Sathapana Bank. For such visits, the CAO case team, external experts, and an interpreter/translator would be expected to participate. Interviews with the relevant officers of MEF, MIFA, North Haven Thai, and Advans is also expected.

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<sup>133</sup> CAO Policy, para. 120.

<sup>134</sup> CAO Policy, paras. 116–117.

## Compliance Investigation Schedule, Timeframe, and Reporting Requirements

According to the CAO Policy,<sup>136</sup> a draft compliance investigation report will be completed within one year of the disclosure of an appraisal report.<sup>137</sup> A draft compliance investigation report for this case will be circulated to IFC Management for factual review and comment. Management may share the draft report with the client on the condition that appropriate measures are in place to safeguard the confidentiality of the draft report prior to public disclosure.<sup>138</sup> IFC will have 20 business days to provide written comments.

At the same time, the draft investigation report will be circulated to the complainants for their factual review and comment, provided that appropriate measures are in place to safeguard the confidentiality of the draft report prior to public disclosure. If such confidentiality measures are not in place, complainants will, at a minimum, receive a draft table of the investigation's findings for factual review and comment and as a source of information to inform future consultations on any IFC Management Action Plan (MAP).<sup>139</sup>

Upon receiving comments on the consultation draft from IFC and the complainants, CAO will finalize the investigation report. The final report will be submitted to IFC senior management and circulated to the Board for information. The Board has no editorial input on the content of a CAO compliance investigation report. Once the investigation report is officially submitted to IFC Management and circulated to the Board, CAO will notify the public on its website of the investigation's completion.<sup>140</sup>

Upon CAO's final submission of the compliance investigation report to IFC, IFC Management has 50 business days to submit a management report to the Board for consideration. The management report must include a MAP for Board approval. A MAP contains time-bound remedial actions that IFC proposes for the purpose of addressing CAO findings of non-compliance and related harm. IFC must consult with complainants and the client during its MAP preparation process, and its management report must also include a reasoned response to CAO's finding or recommendations regarding non-compliance or related harm that IFC is unable to address in the MAP.<sup>141</sup>

CAO will submit comments on the proposed MAP to the Board, and the complainants may submit a statement to CAO on the proposed MAP and the adequacy of consultations for circulation to the Board.<sup>142</sup> Upon the Board's approval of the MAP, the compliance investigation report, management report, and MAP will be published on CAO's website.<sup>143</sup>

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<sup>136</sup> CAO Policy, para. 121.

<sup>137</sup> As an interim measure toward implementation of the CAO Policy timelines, in FY24 CAO will complete draft compliance investigations within 18 months of the disclosure of an appraisal report.

<sup>138</sup> CAO Policy, para. 122.

<sup>139</sup> CAO Policy, para. 124–125

<sup>140</sup> CAO Policy, paras. 123, 127–129.

<sup>141</sup> CAO Policy, paras. 130–132, 134.

<sup>142</sup> CAO Policy, para. 135.

<sup>143</sup> CAO Policy, para. 138.