



**April 23, 2018**  
*Office of the Compliance Advisor Ombudsman (CAO)*

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## **TERMS OF REFERENCE**

*CAO Compliance Investigation of IFC's Investment in Axzon, Ukraine*

*Project #31990*

*Complaint 01*

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### **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 two private sector arms of the World Bank Group, the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA). CAO 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 the IFC and MIGA.

If CAO concludes that the parties are not willing or able to reach a facilitated solution, the case is transferred to the compliance function of CAO, to appraise whether the concerns raised in the complaint merit a compliance investigation of IFC/MIGA.

The focus of CAO Compliance is on IFC and MIGA, not their client. This applies to all IFC's business activities including the real sector, financial markets, and advisory services. CAO assesses how IFC/MIGA assured itself/themselves of the performance of its business activity or advice, as well as whether the outcomes of the business activity or advice are consistent with the intent of the relevant policy provisions. In many cases, however, in assessing the performance of the project and IFC's/MIGA's implementation of measures to meet the relevant requirements, it will be necessary for CAO to review the actions of the client and verify outcomes in the field.

CAO discloses the findings of its compliance investigation in an investigation report to inform the President and Board of the World Bank Group, senior management of IFC/MIGA, and the public about its decision.

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

### **Background to the Investment**

Axzon Group is an agricultural and food production company operating in Denmark, Poland, Ukraine and Russia. In May 2013, IFC approved: (i) a senior loan of up to EUR36 million to Axzon and (ii) an equity investment of up to DKK134,137,081 (approximately USD23 million) in Axzon A/S holding company. The purpose of the investment was to support expansions and acquisitions in Poland, Ukraine and Russia. The loan was fully prepaid in June 2017. Additionally, IFC committed to an A-loan of EUR10 million in August 2016, which was subsequently cancelled in July 2017. However, IFC's equity investment remains active.

## The Complaint

In February 2014, CAO received a complaint regarding the impacts of Danosha Ltd., a subsidiary of Axzon Group (both referred to as “the client”). Danosha is a vertically integrated pork producer from grain cultivation to the sale of live pigs for processing bred in seven farms across the Ivano-Frankivsk region of western Ukraine. The complaint was filed by community members from Sivka-Voynylivska village, in Kalush district, and from Delievo and Lany villages, in Halych district. The complaint was supported by the National Ecological Centre of Ukraine. In February 2017, CAO received a supplement to the complaint from community members from the same villages with support from the Environment People Law organization. The complaint is accessible on CAO’s website.<sup>1</sup>

The complaint alleged violations of IFC’s environmental and social (E&S) standards and adverse environmental and social impacts across 7 overlapping issues:

- i. **Environmental and social and management system:** concerns about the adequacy of the environmental and social impact assessment (ESIA) for the Danosha farms.
- ii. **Air, water, and soil pollution:** swine operations causing air pollution and strong odors which is affecting the health and well-being of the public.
- iii. **Water extraction:** drying of wells and groundwater depletion partly attributed to water extraction for the client’s operations.
- iv. **Halych national nature park:** concerns about potential impact on the park and failure to consult with the protected area representatives.
- v. **Road-related impacts:** vehicle traffic in relation to the project has led to vibrations causing structural damages to nearby houses and buildings; and dust emissions are impacting public health and well-being.
- vi. **Land use and associated compensation:** Lack of prior agreement and adequate compensation for private land plots being used for client’s operations.
- vii. **Stakeholder engagement and grievance mechanism:** inadequate stakeholder engagement throughout project planning, development, and operations.

In April 2018, CAO released a compliance appraisal in relation to the complaint, and decided to conduct a compliance investigation of IFC’s E&S performance in relation to the project.

## Scope of the Compliance Investigation

The focus of this CAO compliance investigation is on IFC, and how IFC assured itself of the environmental and social performance of its investment at appraisal and during supervision.

The approach to the compliance investigation is described in the CAO Operational Guidelines (March 2013), and states that the working definition of compliance investigations adopted by CAO is as follows:

*An investigation is a systematic, documented verification process of objectively obtaining and evaluating evidence to determine whether environmental and social activities, conditions, management systems, or related information are in conformance with the compliance investigation criteria.*

As set out in CAO’s appraisal report, CAO will conduct a compliance investigation of IFC’s investment in the client in relation to the issues raised in the complaint.

The compliance investigation will consider whether IFC’s investment in the client was appraised, structured and supervised in accordance with applicable IFC policies, procedures and standards.

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<sup>1</sup> See [http://www.cao-ombudsman.org/cases/case\\_detail.aspx?id=218](http://www.cao-ombudsman.org/cases/case_detail.aspx?id=218).

It will also consider whether IFC's Policy and Performance Standards on Environmental and Social Sustainability and Policy on Disclosure of Information as applied to this project provide an adequate level of protection.

In the context of IFC's E&S policies, Performance Standards and procedures, CAO's investigation will focus on the adequacy of:

- IFC's review and supervision of the client's ESMS, including measures to ensure that procedures are in place to test for, and mitigate against, environmental pollutants;
- IFC's review of the (i) ESIA documentation (including water extraction, carrying capacity and manure management system) and (ii) associated consultation and disclosure, where relevant.

## **Compliance Investigation Process and Preliminary Timeline**

The preliminary time schedule is for CAO to have a draft compliance investigation report ready by September 2018.

A draft Investigation Report will be circulated to IFC senior management and all relevant IFC departments for factual review and comment. IFC comments should be submitted in writing to CAO within 20 working days of receipt by IFC.

Upon receiving comments from IFC on the consultation draft, CAO Compliance will finalize the report. The final report will be submitted to IFC senior management for official response. A notification will be posted on CAO's website. IFC has 20 working days to submit a written response to CAO. CAO will forward the investigation report and the IFC response to the President of the World Bank Group. The President has no editorial input as to the content of the compliance Investigation Report, but may take the opportunity to discuss the investigation findings with CAO.

Once the President is satisfied with the response by IFC senior management, the President will provide clearance for the Investigation Report and the response. The President retains discretion over clearance. After clearance, CAO will disclose the investigation report and the IFC response to the Board. CAO will also alert relevant stakeholders of the disclosure of both documents on CAO's website, and share the documents with the complainants.

## **External Panelists**

As per its established practice, CAO will engage one or more external experts to work with it on this task. For this compliance investigation, CAO considers the following as necessary for the compliance investigation panel:

- Expertise in agri-business operations, including the assessment and management of risks related to industrial pig-farming, manure management, water extraction, land and air emissions in Ukraine;
- Expertise in Ukrainian environmental laws in relation to permitting required for agri-business operations, emissions and pollutants testing.
- Knowledge of IFC's E&S policies, standards and procedures, in particular Performance Standards 1, 3, and 4.
- Experience and knowledge relevant to the conduct of compliance investigations.
- Demonstrated ability to analyze policies and practices and develop proposals for reform in complex institutional contexts.