



FINAL OMBUDSMAN ASSESSMENT

TRANSFER TO COMPLIANCE

India/Mahindra Farm Services-01,-02,-03,-04/Confidential

Complaints Regarding
the Mahindra ShubhLabh Services Ltd. (MSSL) project

March 27, 2008

Office of the Compliance Advisor/Ombudsman
International Finance Corporation/
Multilateral Investment Guarantee Agency

Final CAO Ombudsman Assessment Mahindra ShubLabh Services, Ltd. (MSSL) Complaints

Between March 2007 and February 2008, the CAO Ombudsman was engaged in negotiations between parties involved in four separate complaints regarding the Mahindra ShubLabh Services, Ltd. (MSSL) project. IFC supported the project in 2002 with a \$2.2 million equity investment for development of 180 Agricultural Service Centers (ASCs) in India, to be developed over a four-year period.

The ombudsman assessment involved multiple interviews, discussions, and e-mail exchanges with the four complainants and with representatives of MSSL and IFC staff and management. The purpose of the assessment was to help the parties clarify the issues raised in the complaints and to decide whether a mutually agreeable resolution was possible.

The four complaints raised the following specific issues:

- The project did not train or educate farmers about the use of eco-friendly pesticides and fertilizers...
- The project promised eco-friendly and organic farming, but only provided traditional agriculture products;
- The project supplied large quantities of pesticide to franchisees and required them to sell it to local farmers;
- Many farmers lost their crops and the fertility of the land was negatively impacted because of excessive use of pesticide provided by the project;
- The project did not, as committed, possess specialized knowledge in agriculture to improve farm productivity, resulting in losses for both farmers and franchisees.
- The project offered no expertise or infrastructure that would add value to people working in the field of agriculture.
- The project offered no knowledge or technical expertise to increase productivity for the farmers.
- The project's commitments were not realized and research to determine its feasibility was not done before launching the concept.
- The farmers suffered heavy losses and were unable to shift and adopt new technologies.

In March 2007, the CAO Ombudsman made an assessment trip to India to meet with the parties and discuss these issues in detail. In July 2007, CAO drafted a preliminary report that described the project, the complaints and their specific allegations, methods and findings of the March 2007 assessment trip, the perspectives and responses of MSSL, and suggested approaches for resolving the complaints. Each of the parties had an opportunity to comment on and clarify the perspectives described in the report before a final draft was distributed to them.

The preliminary report was intended to help the parties better understand the issues and perspectives and identify possible solutions. The CAO did not publicly release the preliminary report at that time, agreeing with the parties to do so only once they had reached agreement on how to resolve the complaints, or had reached an impasse in negotiations triggering a CAO Compliance appraisal. That report is now publicly available.

On January 30, 2008, MSSL informed the CAO Ombudsman that it did not wish to negotiate, unless the complainants were willing to re-consider the company's terms for resolution.

After contacting the four complainants to discuss and assess MSSL's final terms, the CAO Ombudsman concluded that a negotiated solution was not possible, and on March 7, 2008, sent written notification to the CAO. IFC senior management were formally notified, and on March 17, 2008, the complaints were transferred to CAO Compliance.

The impasse between the parties involved a difference of opinion in the type of third-party assistance that should be engaged to resolve the complaints.

MSSL requested the cases be settled through arbitration, while the complainants requested mediation. Throughout the negotiations, MSSL maintained it was open to one-on-one meetings with the complainants in the presence of CAO and IFC. MSSL did not wish to engage in a formal mediated process, or in the alternative process of "med-arb" (mediation-arbitration) suggested by CAO. (Med-arb is a process whereby parties first attempt to resolve disputes through mediation, with any outstanding or unresolved issues then decided by a three-member arbitration panel.)

The complainants say the franchise agreement, which they consider to be complicated and legalistic, would limit the scope of an arbitration to specific contractual issues, and that issues of compliance with IFC's social and environmental commitments would not be ruled on by an arbitrator. They also believe their inability to pay for legal representation or legal advice prior to and during an arbitration would result in a confusing or untrustworthy process. Although the complainants acknowledge signing an agreement that was not fully understood by them, they said they believed the World Bank Group's backing of the project implied a high likelihood of success, and low probability of negative social and environmental outcomes.

The negotiations throughout this assessment were extensive and complex, due in part to the number of parties and their separate geographic regions in India, in part to the country's economic conditions, and in part to a lack of clarity about the IFC's distinction between social impacts versus commercial impacts.

Regarding the latter, IFC project management and staff argue that the cases are commercial in nature – as the complainants were franchisees who entered into a contractual agreement – and therefore should not fall within the purview of the CAO, whose mandate is to address environmental and social impacts of IFC/MIGA investments.

The CAO determined, however, that the four complaints met CAO's eligibility criteria for the following reasons:

- The complaints pertain to a project that IFC/MIGA is participating in;
- The issues raised in the complaint pertain to the CAO's mandate to address environmental and social impacts of IFC/MIGA investments;
- The complainants may be affected if the social and/or environmental impacts raised in the complaint occurred.

Both the complainants and the sponsor described and offered evidence to the CAO Ombudsman that the intended outcomes of the project were not achieved, and failure of the original business model resulted in negative social outcomes. Further evidence of this is included in two letters signed by a number of farmers involved in the MSSL franchise of one of the four complainants. The letters, dated January 2008, were directed to CAO and to the IFC in support of the former franchisee who filed the complaint to CAO.

The IFC does not refute that the project failed to meet its intended goals, and has stated that many IFC-backed business models similarly do not succeed as intended.

The original IFC-supported project sought to establish ASCs in 180 locations around India. Soon after its launch, an estimated 55 people who purchased ASC franchisee agreements closed their shops, having never, or only briefly, served the poor and low-income farmers the ASC project was intended to benefit.

In an effort to recoup its losses and keep the company afloat, MSSL said it abandoned the ASC concept and re-established itself as a marketer and distributor of pesticides and other agrichemicals.

According to IFC, the service centers were intended to provide farmers with a one-stop shop that would supply (i) appropriate inputs such as seed, fertilizers, and pesticides, (ii) rental equipment, (iii) information on agriculture techniques and market information, (iv) contractual farm input application and advisory services, and (v) access to crop finance from commercial banks.

IFC's 2002 Environmental Review Summary says the objective of the project's business model is "to improve farming profitability and sustainability by increasing agricultural yields, and reduce production costs and chemical pest control dependency... Moreover, the project will benefit the health and well being of farmers and the environment by promoting integrated pest management, non-chemical methods and informed management of chemical products."

As part of the assessment, the CAO Ombudsman recommended the IFC engage with its client and participate in a mediated dialog aimed at resolving the issues. IFC stated that its participation in or encouragement of mediation to resolve a complaint against a client is outside accepted business practice, and could result in reputational risk.

In the absence of an agreement among the parties to negotiate the issues, and in accordance with CAO's Operational Guidelines, the complaints have been transferred to CAO Compliance for appraisal.