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## COMPLIANCE MONITORING REPORT

*IFC Investment in Avianca S.A., Colombia  
Project #25899*

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**Monitoring of IFC's Response to:  
CAO Investigation of IFC Investment in Avianca S.A., Colombia**

**May 10, 2017**  
*Office of the Compliance Advisor Ombudsman (CAO)*

## 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 IFC and MIGA.*

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

CAO's compliance function oversees investigations of IFC/MIGA's environmental and social performance, particularly in relation to sensitive projects, to ensure compliance with policies, standards, guidelines, procedures, and conditions for IFC/MIGA involvement, with the goal of improving IFC/MIGA environmental and social performance.

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

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## **Introduction**

The CAO compliance function oversees investigations of IFC and MIGA with a view to improving the environmental and social (E&S) performance of the institutions.

Following a CAO compliance investigation, CAO may determine that it is necessary to monitor actions taken by IFC or MIGA until such actions assure CAO that its compliance findings are being addressed.<sup>1</sup>

This report documents CAO's monitoring of its *Investigation of IFC Investment in Avianca S.A., Colombia* (the investigation), which was finalized in April 2015.<sup>2</sup>

## **Background and Complaint**

Avianca ("the client") is one of the largest airlines in Latin America and the largest in Colombia, operating from its main base at El Dorado International Airport, Bogota. IFC invested in the company in 2009 with a view to supporting it to renew its fleet, reduce costs, improve efficiency and safety as well as provide better passenger service. IFC's commitment to the company totaled US\$50 million comprising a subordinated (or C) loan of US\$15 million disbursed in November 2008, and a straight senior (or A) loan of US\$35 million disbursed in July 2009.

In November 2011, CAO received a complaint regarding IFC's investment in the client from the International Trade Union Confederation (ITUC) in cooperation with the International Transport Workers Federation (Global Unions) and national level unions (ACAV/ACDAC and SINTRAVAL) representing employees of the client. The complaint raised a number of allegations relating to the client's compliance with IFC Performance Standard 2 (PS2) – Labor and Working Conditions.

CAO issued terms of issued Terms of Reference (TOR) for the investigation in April 2013. The TOR required CAO to address the following issues:

- a. whether IFC exercised due diligence in its review and supervision of the PS2 risks attached to the Project; in particular
  - whether IFC's approach to PS2 issues during the E&S review process was commensurate to risk and otherwise compliant with relevant policies and procedures;
  - whether IFC was in a position to make an informed judgment as to the likelihood that the investment would meet the requirements of PS2 prior to disbursement; and
  - whether IFC's record of supervision constituted an adequate and timely response to specific concerns being raised by unions regarding the client's PS2 performance.
- b. whether IFC policies, procedures and staffing structures provide a robust framework for the advancement of the objectives of PS2 in its clients.

The TOR included in the scope of the investigation "developing an understanding of the immediate and underlying causes for any non-compliance identified by the CAO."

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<sup>1</sup> CAO Operational Guidelines 2013, Section 4.4.6, available at: <https://goo.gl/m0mGUv>.

<sup>2</sup> The CAO investigation, IFC's response to the investigation, and related materials are available on the CAO website: <https://goo.gl/yAs8Re>.

## CAO Investigation Findings

The investigation made a number of non-compliance findings in relation to IFC's review and supervision of E&S aspects of the project. These are summarized in the table below.

CAO Investigation Findings	
<b>A. Environmental and Social Review</b>	<ul style="list-style-type: none"><li>• IFC's pre-project E&amp;S review in relation to labor issues was not commensurate to risk.</li><li>• IFC's E&amp;S review did not ensure that its client had conducted an integrated process of E&amp;S assessment that covered "all relevant E&amp;S risks and impacts of the project" including PS2 issues.</li><li>• IFC did not adequately analyze its client's "commitment and capacity" in relation to PS2 compliance.</li><li>• IFC did not have sufficient basis to support the assertion contained in its Board paper that its client was in compliance with PS2.</li><li>• In the context of an ongoing dispute between the client and some of its unions, significant country governance risks in relation to Freedom of Association, and in the absence of consultation with the complainant unions as part of project preparation, it would have been consistent with the IFC Sustainability Framework to require more stringent due diligence prior to commitment.</li><li>• It would have been consistent with PS1 for IFC to have included as conditions of commitment or disbursement, specific disclosure requirements, and a requirement to agree on an Action Plan addressing the findings of the Labor Assessment following consultations with workers and their representatives.</li></ul>
<b>B. Disbursement</b>	<ul style="list-style-type: none"><li>• IFC did not give appropriate consideration to the adequacy of the initial Labor Assessment prior to disbursement. As a result the basis for IFC's engagement with its client around PS2 issues was significantly weakened.</li><li>• This situation compounded problems with the structure for supervision of the project that stemmed from weaknesses in the terms of reference (TOR) for the Labor Assessment and the conditions of disbursement (CODs) incorporated into the Loan Agreement.</li><li>• IFC's July 2009 disbursement was made without sufficient basis to meet the requirement of the Sustainability Policy that "IFC does not finance new business activity that cannot be expected to meet the Performance Standards (PSs) over a reasonable period of time."</li></ul>
<b>C. General Supervision</b>	<ul style="list-style-type: none"><li>• IFC did not "develop and retain the information needed to assess the status of [its client's] compliance with the Performance Standards" (PSs) as required by the Environmental and Social Review Procedures (ESRP).</li><li>• Lacking an adequate information basis on which to assess the status of the client's compliance; absent effective leverage and without appropriate tools at its disposal, IFC made limited progress in addressing the issues which formed the basis of the unions' complaint to CAO.</li></ul>

<b>CAO Investigation Findings</b>	
<b>D. Disclosure and Consultation</b>	<ul style="list-style-type: none"> <li>• IFC did not adequately supervise the requirements that its client:           <ul style="list-style-type: none"> <li>(a) disclose the findings of its Labor Assessments;</li> <li>(b) engage in “effective consultation” as part of the preparation of either its Labor Assessments or the resulting Action Plans, in particular the requirement that effective consultation should be based on the “prior disclosure of … draft documents and plans;” or</li> <li>(c) disclose Action Plans, updated versions of the Action Plan, and report regularly on progress against its Action Plans.</li> </ul> </li> </ul>
<b>E. Adequacy of IFC policies, procedures and staffing structures</b>	<ul style="list-style-type: none"> <li>• IFC’s implementation of PS2 suffered from limitations in three key areas:           <ul style="list-style-type: none"> <li>(a) depth and expertise of E&amp;S staff on PS2 issues;</li> <li>(b) methodology for pre-investment PS2 review; and</li> <li>(c) leverage, tools and other resources for effective supervision.</li> </ul> </li> </ul>

## **Monitoring Methodology**

This report is based on information provided to CAO by IFC and by the complainants, as well as a review of documents available to CAO as of April 2017, including:

- a. IFC’s Response to the IFC investigation issued in May 2015 (the IFC Response);
- b. Updates and documentation provided to CAO by IFC in June 2016, in November 2016, and in March 2017;
- c. Updates provided to CAO by the Complainants in September 2016; and
- d. Other publicly available documentation.

## **Update on Labor Issues at the Project Level**

CAO's investigation covered the period May 2007 to December 2013. In February 2015, the Colombian Constitutional Court issued a decision against the client on freedom of association grounds and ordered that the client extend the benefits of the voluntary benefits plan to all workers, and that those who had accepted the voluntary benefits plan should be permitted to join the union.<sup>3</sup> As a result, the court ordered that the client should make certain payments to workers. The complainants reported that the sum ordered was in the order of USD 2 million.<sup>4</sup> The client reported that it had made a payment to all members of ACDAC and ACAV on June 10, 2015 in compliance with the court order.<sup>5</sup>

In September 2016, the complainants reported to CAO that they had not had any contact with IFC in relation to the investigation report or the IFC response. The complainants did, however, report some improvements in their engagement with the client in relation to labor issues.

## **Update on Actions Taken by IFC**

In May 2015, IFC published a management response in relation to the CAO investigation.<sup>6</sup> The response included a number of comments and observations in relation to CAO's findings. IFC noted that it remained "committed to continuous learning and improvement of [its] E&S risk management practice." IFC noted that it had already made procedural and organization changes to improve in this area, including:

- a. capacity building and training of E&S specialists on assessing and managing labor-related risks;
- b. developing internal and external guidance on managing labor issues;
- c. relying on the support of independent labor experts; and
- d. having regular interaction with Global Unions.

IFC's response did not include any commitment to specific actions in response to CAO's findings either at the project level or in terms of policy and practice. At the project level this was explained on the basis that the client had prepaid its loan to IFC in December 2013.

During the supervision period, IFC provided further detail to CAO in relation to the actions it had taken at an institutional level to address PS2 issues:

- a. *Engagement with Global Unions*: IFC reported that it has ongoing constructive dialogue with ITUC/Global Unions on labor concerns that are raised directly by them or their constituents, including regular meetings with ITUC/Global Unions representatives in Washington D.C.
- b. *External Labor Consultants*: IFC reported that, since 2014, it has engaged an international labor consulting firm to provide "on call" support and guidance to IFC staff and clients on projects with complex or high-risk labor issues. IFC reported that, as of June 2016,

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<sup>3</sup> República de Colombia, Corte Constitucional, Sentencia T-069/2015, available at: <https://goo.gl/z6ddgh>.

<sup>4</sup> Press Release, "Colombian court orders Avianca to pay workers cheated by decade of anti-unionism," June 17, 2015, available at: <https://goo.gl/BOqlrA>.

<sup>5</sup> US Securities and Exchange Commission, Form 20-F Annual Report, Avianca Holdings S.A., p. 18 available at: <https://goo.gl/VGKQIZ>.

<sup>6</sup> "IFC Management Response to CAO's Investigation Report on IFC's Investment in Avianca," May 5, 2015, available at: <https://goo.gl/a2Kvm8>.

consultants had provided guidance to project teams on 49 individual projects, ranging from technical support for IFC E&S specialists on complex labor issues to site visits and direct client engagement. Issues addressed through this support include: contractor management, demobilization and community impact, termination of employment, overtime, retrenchment, discrimination related to retirement age, human resources policy review, employee rights in concession agreements, and contractor management.

- c. *Guidance:* In collaboration with its contracted consultants, IFC reported that it has developed several guidance notes on various labor topics, including internal guidance for IFC staff related to: grievance mechanisms, addressing child and forced labor in the supply chain of retailers, addressing sexual harassment, Turkey and Egypt labor country profiles, freedom of association in Mexico and Central America, freedom of association in EMENA, retrenchment in EMENA and overtime management, including PS2 requirements in Concession Agreements, and including PS2 requirements in EPC contracts. Guidance and information on latest developments on this topic have been disseminated to the IFC E&S team through labor newsletters.
- d. *Training:* In addition to tailored guidance at the project level, IFC reported that its labor consultants have provided training on PS2 for E&S staff including a one-day training for the entire team in 2013, a one day regionally focused training for staff in EMENA in 2015, as well as web-based training in 2014.
- e. *Regional Focal Points Network PS2:* IFC reported that a focal point for PS2 issues has been appointed from the E&S team in each region. These individuals have agreed to be the go-to person for labor issues, providing support to regional staff and information on additional resources.
- f. *Contextual Risk Identification:* Building on lessons from the investigation, as well as other CAO cases, IFC reported that it intended to launch in Q1 FY17 internal procedural requirements for the more systematic screening and documentation of contextual risks at appraisal and during supervision, focusing on country, regional, and sectoral risks. This process is also intended to support the early identification of broader contextual risks relating to labor, as was raised in the investigation:
  - IFC's Environmental and Social Review Document (ESRD) is an internal record of investment project E&S milestones and key decisions from appraisal through supervision. In January 2017, the ESRD template was updated to incorporate a series of prompts for both direct investments and financial intermediary (FI) investments. Contextual risk analysis is now mandatory for E&S Specialists to complete. In relation to PS2, in particular, the ESRD lists "Labor" as a potential contextual risk, and includes US Department of Labor and ILO Reports as potential resources for contextual risk identification.
  - IFC reported that numerous references to contextual risk will be included in a forthcoming update to the Environmental and Social Review Procedures, due for public release in the coming months. Language reviewed by CAO included contextual risks among those to be taken into account at each project stage. In particular, in relation to direct investments, significant sectoral or regional contextual risks should inform provisional E&S risk categorization, and should be discussed when investments are reviewed for approval. For large, complex, or transformational projects with a high degree of contextual risk, E&S staff will consult with the World Bank as appropriate.

- g. *Conditions of Disbursement (COD) Clearance:* IFC's new project management software will provide a formal process for collecting and recording E&S Specialist intervention on CODs related to E&S requirements. IFC expected that a new workflow would be implemented in the software by March 2017. This is intended to formalize what has historically been an informal exchange between the investment and E&S team members. When a disbursement is processed in the system, CODs based on E&S requirements will include an additional step for approval. The COD template will have a check box that will allow the Investment Officer or Portfolio Officer responsible for a project to request formal clearance and justification from the Lead E&S Specialist (LESS). The LESS will receive an email notification to "clear" or "not clear" the condition, and will be prompted to provide justification for that choice. If the COD is not cleared at this time, the LESS can revisit the clearance if the condition is later met or waived.

IFC noted that it believes these initiatives have substantially strengthened the awareness and capacity of IFC E&S staff to identify and manage labor risks and impacts as they arise early in the appraisal process or during supervision. IFC also acknowledged that there will be room for improvement and continuous learning / capacity building on PS 2 issues.

## **Monitoring Conclusions**

IFC does not report any actions taken to address CAO's findings at the project level. IFC explains this decision on the basis that the client had prepaid its loan to IFC in December 2013.

IFC has, however, reported institutional changes which partially address CAO's non-compliance findings relating to the adequacy of IFC's policies, procedures, and staffing structures as applied to this investment.

CAO is not assured that the measures proposed by IFC fully address the investigation findings. Beyond the actions outlined in this report, CAO sees benefit in IFC reporting publicly on measures it is taking to address CAO's findings at a systemic level, including:

- a. disclosure of its new procedural requirements for screening and documentation of contextual risks, and elaboration on their application to labor issues and freedom of association;
- b. guidance IFC provides to staff about engagement with workers and their organizations when PS2-related assessments and action plans are developed.

CAO also sees benefit in consultation with representatives of the union movement at the national and international level in relation to these issues.

Overall CAO finds that IFC's response to this compliance investigation has only partially addressed its compliance findings. Nevertheless, CAO has decided to close its monitoring of the investigation considering the time that has passed since the client's repayment of the IFC loan, and IFC's decision not to engage in a project level response with its former client or the complainants. Findings from CAO's investigation that require a response at the level of IFC's policies, procedures and practices may be addressed through CAO's ongoing compliance and advisory work.