

June 27, 2019

Mr. Osvaldo L. Gratacós
Compliance Advisor Ombudsman
International Finance Corporation
2121 Pennsylvania Avenue, N.W. Washington
DC 20433

Subject: IFC Management Response to CAO Investigation Report in relation to IFC investment in Reventazón HPP, in Costa Rica (Project #31383)

Dear Mr. Gratacós:

Thank you for the opportunity to respond to the CAO Compliance Investigation Report (“CAO Report” or the “Report”) concerning IFC’s investment in Reventazón Hydro Power Project (HPP) in Costa Rica (“Reventazón” or the “Project”).¹ This investment supported the State-Owned Enterprise (SOE) *Instituto Costarricense de Electricidad* (ICE) to construct and operate Reventazón. This 305.5 MW hydroelectric power plant was designed to alleviate Costa Rica’s medium-term energy security concerns by displacing fossil fuel-based power with a reliable renewable electric power source that will reduce greenhouse gas emissions and help make Costa Rica become the first Latin American country to run entirely on renewable power.

The Project implemented several best-in-class E&S practices, including: enhancements to an ecological corridor considered Critical Habitat for jaguars and other large felines²; the first-ever aquatic-offset to achieve no loss of Natural Habitat; a Payment for Ecosystems Services scheme^{3,4}; and a methodology to measure GHG emissions from the reservoir. Reventazón won the 2019 Blue Planet Prize, awarded every two years in the context of the International Hydropower World Conference to projects that demonstrate excellence in sustainable development.⁵

IFC recognizes the CAO’s positive confirmation of the thorough due diligence, monitoring process, and measures IFC took to monitor Reventazón’s compliance with diverse and complex E&S issues. CAO has focused its Report specifically on land acquisition, related consultation, information disclosure, and grievance handling. As noted in the CAO Report, when IFC started its appraisal, land acquisition and expropriation had already commenced in accordance with national law. ICE additionally undertook significant efforts to meet IFC’s Performance Standard (PS) requirements by: (i) halting any further land acquisition or expropriation until a PS5-compliant Resettlement Framework/Plan (RFP) had been developed and approved by the Lenders; and (ii) taking special care in protecting vulnerable project affected people. ICE was committed to meet PS5, and implemented several measures to support livelihood restoration of vulnerable landowners, including

¹ The information in this letter and its enclosures is provided solely in the context of the CAO process which is an independent office that reports directly to the President of the World Bank Group. The CAO is not a court or legal enforcement mechanism and nor is CAO a substitute for international court systems or court systems in host countries. Nothing contained herein nor in CAO’s reports constitutes evidence or gives rise to any legal claims against IFC or is intended as a waiver of any of IFC’s privileges and immunities under its Articles of Agreement or any other applicable law, and IFC reserves all rights.

² <https://youtu.be/2xq61e-QeYM>

³ The Payment for Ecosystem Services was based on a scheme developed by the IBRD over a decade earlier to assess and manage watershed-wide impacts and risks and support of afforestation, reforestation and sustainable land practices.

⁴ <https://youtu.be/2xq61e-QeYM>

⁵ <https://www.hydropower.org/iha-blue-planet-prize>

assistance in both acquiring replacement land and restoring productive activities. We appreciate CAO's acknowledgment of ICE's efforts to meet IFC's requirements.

The Reventazón land acquisition impacted a total of 136 properties affecting 62 households. Nineteen of these households were considered vulnerable because they were at risk of losing their livelihoods as a result of the Project's land-take.⁶ PS1 requires IFC clients to "identify individuals and groups that may be directly and differentially or disproportionately affected by the project because of their disadvantaged or vulnerable status" and to "implement differentiated measures"⁷ for these vulnerable project-affected people. In monitoring Reventazón, IFC focused on client efforts to safeguard vulnerable project affected people's livelihoods by restoring or improving against pre-project conditions. Both the lender-required Resettlement Completion Audit (RCA) and CAO's Report confirmed that impacts on vulnerable project affected people were managed in compliance with PS5.

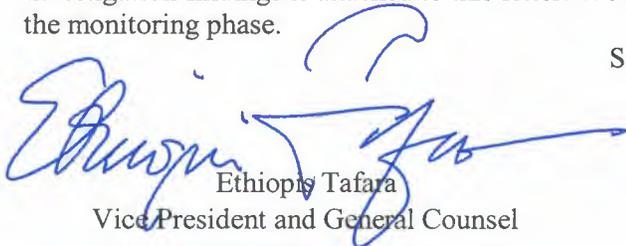
IFC notes the CAO report observation that IFC did not apply the same attention to the monitoring of ICE's management of impacts on companies or landowners classified as non-vulnerable project affected people compared to the companies or landowners classified as vulnerable. The same monitoring of Project compliance with the agreed measures, including compensation and support required by the PSs, is to be applied irrespective of the vulnerability assessed for the individuals or groups. Accordingly, following the RCA and CAO Report, IFC has enhanced its monitoring related to Reventazón's implementation of PS5, including asking ICE to collect additional data regarding the individuals considered non-vulnerable.

This data collection confirmed that compensation was negotiated and agreed with a majority of owners, for which ICE provided evidence that livelihoods were not negatively affected. For the remaining fifteen non-vulnerable owners, ICE, at IFC's request, is currently undertaking a detailed review to assess whether livelihoods and income sources were substantially affected by the Project. If needed, corrective actions will focus on livelihood restoration, such as technical assistance to support productive activities, capacity building programs, social assistance, and legal support. IFC will review the land valuation methodology used by ICE and local courts in comparison with PS5 requirements. IFC will continue to monitor the establishment of Corrective Actions to restore livelihoods and income where issues are identified, with a focus on the remaining fifteen owners classified as non-vulnerable.

At a broader level, IFC recognizes the challenges inherent in land acquisition and resettlement. IFC intends in future hiring to include additional social specialists with experience to increase coverage of complex social issues in projects, including PS5. Appreciating the particular challenges clients sometimes face implementing PS5, IFC will develop specific guidance for teams working with such clients, including early engagement and flagging of challenging issues. Where clients face constraints in providing compensation exceeding that mandated by local regulation, teams will explore alternate compensation options, such as in-kind compensation either in the form of alternative land, technical assistance, or other services.

IFC welcomes the feedback on its due diligence and monitoring performance and, along with its client, remains committed to engaging with relevant project stakeholders. A complete and itemized response to CAO's key investigation findings is attached to this letter. We look forward to continuing our dialogue with CAO during the monitoring phase.

Sincerely,



Ethiopia Tafara
Vice President and General Counsel



Stephanie von Friedeburg
Vice President and Chief Operating Officer

⁶ Disadvantaged or vulnerable status may stem from, *inter alia*, factors such as "poverty or economic disadvantage, and dependence on unique natural resources." PS1, footnote 18.

⁷ PS1, paragraph 12.

Annex. IFC Tabulated Management Response: Reventazón HPP in Costa Rica (Project #31383)

	CAO Compliance Assessment	Nature of Compliance	IFC Response with Actions Taken or Proposed	Expected Timeline
Approach to Land Acquisition and Livelihoods Restoration				
<i>Negotiation Process and Expropriation</i>				
1.	<p>CAO finds that IFC’s review overlooked the risk that the company would rely on the continued use of expropriation to complete its land acquisition program at the expense of negotiating settlements. IFC’s review also lacked an analysis of ICE’s expropriation law against the requirements of PS5, as required by PS5 paras 30-31. Of particular concern were the provisions of national law that allowed ICE to take possession of land in advance of paying compensation, and without an opportunity given to reach negotiated settlements (cf. PS5 paras 3 and 9). CAO further finds that, despite a growing recourse to expropriation as project construction and the land acquisition process advanced, IFC did not take action to encourage the avoidance of expropriation as required by PS5, para. 3.</p>	<p>Sufficiency of IFC due diligence and monitoring of PS5 compliance, both in terms: (i) of IFC’s analysis of expropriation law against PS5; and, (ii) client’s implementation of the PS5-recommended preference of negotiated settlement over expropriation (PS5).</p>	<p><u>Project Level:</u> Though IFC did make efforts to understand and document the gaps between local law and PS5 during the appraisal and as part of the approved RFP, this analysis could have been more comprehensive. PS5 requirements for all the owners, including those classified as non-vulnerable, could have been better articulated as actionable requirements in the RFP to fully align with PS5. The attention devoted to ensuring compensation in line with PS5 for owners considered as vulnerable resulted in less focus on supervising ICE’s management of impacts on companies or landowners considered as non-vulnerable, whose livelihoods did not depend on the land acquired by the Project. IFC is committing to additional actions on this issue, as detailed below in response #4.</p> <p>ICE faced particular constraints regarding land acquisition relating to timing of compensation in relation to expropriation. Although ICE was permitted by law to take possession of land in advance of paying compensation, ICE only resorted to expropriation where the owners rejected the initial compensation offer. ICE took possession of the land after the compensation offered to the owners was put into an escrow account accessible by the owners at any time during the process. This is standard and recognized practice, mentioned in PS5’s Guidance Note, paragraph 9.</p> <p><u>Systemic Level:</u> IFC recognizes that clients may sometimes face particular challenges in exceeding the requirements of expropriation and</p>	<p>See response #4</p> <p>December 2019</p>

			<p>eminent domain laws, especially regarding cash compensation. To support teams working with clients facing such constraints, IFC will develop guidance on working with such clients, such as engaging with these clients early on in the process, highlighting increased PS5-compliance risks and challenges, and reflecting the need for enhanced due diligence, risk management framework, and monitoring. In these instances, teams will inform the client of alternative compensation options, including in-kind compensation and offering technical assistance or other types of services to affected landowners.</p>	
Land Pricing				
2.	<p>CAO finds that IFC did not ensure that the land pricing methodology developed in the RPF and PRCV met PS5 requirement for “compensation for loss of assets at full replacement cost and other assistance” (para. 9). While additional forms of assistance were envisaged for vulnerable landowners, the company’s approach to land pricing for non-vulnerable groups relied on estimations of market land values and contrary to the objectives of PS5, IFC did not ensure that the methodology used included replacement value and additional assistance designed to ensure that displaced landowners were not left worse off.</p> <p>CAO further finds that, as the land acquisition program advanced, and despite concerns being raised about under-compensation by affected landowners, the IESMC, and the RCA, IFC did not require its client to</p>	<p>Sufficiency of (i) IFC’s due diligence of ICE’s land pricing methodology with regard to PS5 requirements for “full replacement cost and other assistance” and (ii) IFC’s monitoring to identify and propose corrective action to any under-compensation (PS5).</p>	<p><u>Project Level:</u> The RFP requested and approved by IFC as a condition of Board Approval requires compensation for loss of assets at full replacement cost and assistance with transaction costs. However, IFC notes the need for ongoing monitoring of Project compliance with agreed measures, including understanding the expropriation methodology against PS5 requirements and monitoring the execution of the RFP for owners considered non-vulnerable.</p> <p>IFC will review the land valuation methodology used by ICE and local courts in comparison with PS5 requirements. Based on this assessment, IFC will engage with ICE about viable Corrective Actions aimed at restoring livelihoods and income where necessary and feasible, with particular focus on 15 identified owners considered non-vulnerable project affected people (see response #4). IFC will also engage with ICE to review its internal procedures and establish a Corporate Land Acquisition and Resettlement Policy consistent with IFC PS5 for its future projects. This policy may include alternative means of compensation that ICE may consider such as in-kind compensation, technical assistance or other similar services.</p>	<p>Methodology and Gap Review – December 2019</p> <p>Agreement on Corrective Actions, as applicable – December 2019</p> <p>June 2020 – set as the date for an update of ICE’s internal procedures and policy</p>

	implement corrective actions to ensure that affected landowners classified as non-vulnerable would be compensated for loss of assets at full replacement cost as per PS5, para. 9. This gives rise to a risk of systemic under-compensation contrary to the requirements of PS5.			
Extent of Land Take				
3.	CAO finds that when the company sought additional land for the management of geological risks, IFC did not ensure that land take was minimized as required by the objectives of PS5 and para. 8. In particular, IFC did not assure itself that the company informed and incorporated feedback from affected landowners to define the extent of land required following the expansion of the geological buffer zone (cf. PS1, para. 31).	Sufficiency of IFC's monitoring (i) whether the client minimized additional land take and (ii) to understand if owners affected by additional land take were consulted and their feedback incorporated (PS5).	<u>Project Level:</u> IFC was not sighted on this additional land take, which occurred after IFC's appraisal. The determination of land affected was based on the requirements of the geological risks and ICE paid compensation according to the RFP. As it was already completed when IFC learned of it, there was limited opportunity to influence the process. However, to support ICE in sharing information with owners regarding the criteria and geological-risk rationale for the additional land take (one of several topics raised by the complainants), the Lenders hired an independent mediator to facilitate dialog and information-sharing among the parties. Unfortunately, as noted in the CAO Investigation Report, this Lender-triggered mediation effort ultimately was unsuccessful.	Lender-triggered mediation July 2016
Baseline Data				
4.	CAO finds that IFC did not ensure that the company collected appropriate baseline data given the need to (a) apply vulnerability criteria to all affected landowners; and (b) identify and manage impacts of land acquisition on all affected landowners.	Sufficiency of IFC's due diligence in requesting the client to collect and act on comprehensive baseline data for all owners (PS5).	<u>Project Level:</u> When IFC initiated its due diligence, the land acquisition and expropriation process had already commenced. However, IFC required ICE to halt any further land acquisition or expropriation until a PS5-compliant RFP was developed and approved by the Lenders. IFC notes that the focus on vulnerable owners did not extend to the monitoring of ICE's management of impacts on companies or landowners considered as non-vulnerable. The	

<p>Although this issue was identified in the RCA, IFC did not require the client to collect additional data.</p>		<p>baseline data collection similarly focused on owners considered vulnerable.</p> <p>IFC has already begun taking action on this issue. IFC required ICE to conduct ex-post visits (October/November 2017) to owners considered non-vulnerable impacted by the Project's land acquisition process. A data collection was conducted with responses from 76 percent of the owners considered non-vulnerable affected by the Project's land-acquisition process to assess basic socioeconomic conditions in comparison to baseline information (collected in 2012). The remaining 24 percent did not participate in the survey – some declined to participate, some could not be contacted, one was a governmental entity, and two were not interviewed to not interfere with current investigations of complaints received by CAO and MICI. The data collection also included questions about land use, adequacy of compensation received and how it was spent, landowners' potential interest in technical assistance programs implemented by ICE to support livelihood activities, and landowners' opinion about the land acquisition process.</p> <p>After reviewing the information provided against the PSs requirement, IFC assessed that no additional actions are required for 28 landowners (representing 65% of the cases) because: (i) they were landowners who declared they were satisfied with the compensation and for whom ICE presented information demonstrating appropriate compensation and livelihood restoration; (ii) the landowners had their claims successfully reviewed by the local courts; or (iii) the information provided by ICE revealed that these were either absentee owners or owners where only a marginal portion of the property was affected, and thus the economic impact was deemed negligible.</p> <p>For 15 landowners (remaining 35% of the cases), IFC requested further information to better assess the PS5 compliance status regarding livelihoods and income</p>	<p>Survey completed November 2017</p>
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			restoration. In March 2019, ICE issued a report with information related to these 15 owners considered non-vulnerable. IFC will review the land valuation methodology used by ICE and local courts in comparison with PS5 requirements. IFC will continue to monitor the establishment of Corrective Actions to restore livelihoods and income where issues are identified, which may include forms of compensation other than cash, as described in point 2 above.	Agreement on Corrective Actions – December 2019
Consultation and Disclosure of Information				
5.	CAO finds that IFC did not ensure that the company's land acquisition process met the consultation and disclosure requirements of PS1 or PS5. IFC did not have assurance that the process was transparent or understandable without a lawyer. IFC also lacked assurance that the timeframes for land acquisition provided by the company allowed non-vulnerable landowners sufficient time to consider their options prior to making a decision.	Sufficiency of IFC due diligence and monitoring of client consultation with all owners impacted by land-take (PS1).	<p><i>Project Level:</i> Expropriation started before IFC involvement. On engagement, IFC required ICE to halt any further land acquisition or expropriation until a PS5-compliant RFP was developed and approved by the Lenders. This RFP included provisions related to consultation and disclosure, though this consultation did not apply retroactively to property-owners that had already entered an expropriation process. All interactions between the ICE team responsible for asset valuation and social management, and owners are registered by ICE.</p> <p>IFC notes the CAO observation that its monitoring efforts were focused on compliance with PS5 for those landowners considered vulnerable. As mentioned in point 2 above, as part of the establishment of a Corporate Land Acquisition and Resettlement Policy, IFC will encourage ICE to devise a land acquisition process which is transparent, in line with the consultation and disclosure requirements of PS1 and PS5.</p>	June 2020
Grievance Mechanism				
6.	CAO finds that IFC did not ensure that grievances about compensation for land acquired from non-vulnerable landowners were addressed through a Grievance Mechanism as required by PS5. Even after the IESMC reported on inadequate management of	Sufficiency of IFC's monitoring of the client's efforts to develop a Grievance Mechanism to receive and address land-related grievances,	<p><i>Project Level:</i> The Grievance Mechanism, as part of the monitoring, similarly focused on owners considered vulnerable. IFC considered the existing Grievance Mechanism in place for operations to be adequate and compliant with PS1. IFC will now continue to monitor its effectiveness for all owners on an annual basis. As part of IFC's engagement with ICE to review its internal</p>	June 2020

<p>grievances, there is no evidence that IFC required the company to manage complaints in a manner consistent with PS5 requirements for a recourse mechanism designed to resolve disputes in an impartial manner (cf. para. 11). This led to significant delays in the resolution of complaints regarding compensation from non-vulnerable landowners, who were required to go through lengthy court proceedings. While CAO notes that the majority of non-vulnerable complainants secured increased compensation from the courts, the lack of an impartial recourse mechanism applying PS5 standards meant that awards did not necessarily reflect PS5 requirements for compensation at full replacement cost.</p>	<p>including from non-vulnerable projected affected people (PS5).</p>	<p>procedures, IFC will encourage ICE to disseminate the use of the Grievance Mechanism to all owners, including the non-vulnerable owners, consistent with PS1.</p>	
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