

January 9, 2018

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

IFC Management's Response to the CAO Investigation Report on Bujagali Energy Ltd and World Power Holdings, Uganda (Bujagali-07)

Dear Mr. Gratacós:

We appreciate the opportunity to review and respond to CAO's investigation report regarding IFC's performance in relation to the transmission line associated with our investment in Bujagali Energy Limited (BEL). We wish to respond to the report here and via detailed comments to CAO's key findings in the attached Annex.

This Bujagali-07 complaint focuses on questions around the adequacy of crop compensation in relation to the construction of the Interconnection Project (IP), a high-voltage transmission line that helped the Bujagali Hydropower Plant (HPP) evacuate electricity within Uganda and to western Kenya. The IP is owned and operated by the Uganda Electricity Transmission Company Limited (UETCL), a company owned by the Ugandan government, which was also responsible for its construction and financing.

The IP was funded by the African Development Bank (AfDB) and Japan International Cooperation Agency (JICA). IFC did not finance the IP. It was identified as an 'associated facility' of IFC's Bujagali HPP investment. Despite UETCL signing a 'Direct Agreement' committing to follow Lenders' environmental and social (E&S) requirements, which is unusual and not required for associated facilities, IFC's legal and financial leverage over UETCL was more limited and less direct than for a direct investment. AfDB, as a direct lender to UETCL, has played the leading role on E&S compliance, with support from IFC and other Lenders to the Bujagali HPP.

The IP required the acquisition of a total of 2,632 plots of land, with some people owning more than one plot over the 100km corridor. Determination of fair crop compensation values acceptable to all parties is typically complex and frequently a major source of project-related complaints. The IP case was no exception, and was further complicated by official compensation rates that varied along the transmission line route. Unexpected high inflation levels also potentially undermined compensation values in the lead up to payment, affecting those who agreed to compensation only later in the process. Most significantly, unprecedented levels of speculation, involving a range of strategies aimed at making false claims for crop damages to gain cash compensation, challenged UETCL's efforts to fairly compensate legitimately affected people. Widespread speculative activity was recognized and reported to be a problem by all key parties early in the process,

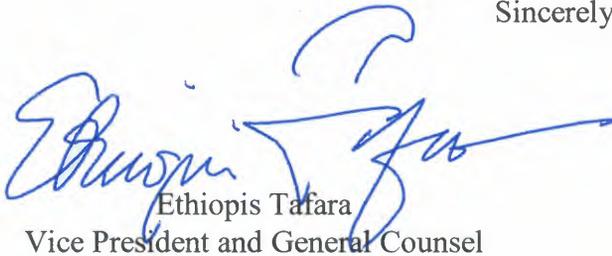
including representatives from villages in the area where the Bujagali-05 and 07 complaints arose, who feared that plot sub-division and sale to ‘outsider’ speculators from nearby towns would hamper the compensation process. Speculative activity took many forms, from late-stage plot sub-division to ‘placing’ of partly grown crops in the ground immediately prior to the survey. Attempts by survey teams to disregard obvious cases of speculation were vociferously opposed by those aiming to benefit.

IFC’s interactions with members of the Bujagali-07 group suggests that their complaint was triggered by the terms of the Bujagali-05 settlement mediated by CAO. In Bujagali-05, a confluence of factors led to UETCL agreeing, on a one-off basis, to compensation rates as high as 2.5 times the original market value of crops. While IFC understands Bujagali-07 claimants’ questioning why they should not also benefit from higher rates arising out of the Bujagali-05 case, we do not believe that these rates represent replacement value for crops as required. This is because the Bujagali-05 settlement included substantial supplemental payments for densely planted young crops deemed by UETCL and the survey teams to have been planted for speculative purposes.

IFC agrees with CAO on the importance of follow-up to confirm that key aspects of IFC and AfDB land acquisition and resettlement requirements were met. To date, UETCL has commissioned an IP project completion report, as well as several other reports and audits dealing with the status of IP land acquisition and compensation. IFC and AfDB have agreed to engage with UETCL to i) identify and address any relevant gaps in these reports vis-à-vis IFC and AfDB completion report requirements, and ii) close out any associated corrective actions.

We appreciate CAO’s detailed review of this complicated project, and look forward to continuing our dialogue with CAO. Please find in the attached Annex further more detailed responses to the key findings raised in the CAO Report.

Sincerely,



Ethiopis Tafara
Vice President and General Counsel



Stephanie von Friedeburg
Vice President and Chief Operating Officer

Annex: IFC Tabulated Management Response: Bujagali-07

| | <i>CAO Finding</i> | <i>IFC Response</i> | <i>IFC Actions Taken or Proposed</i> |
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| 1. | <p>IFC properly recognized the interconnection project as an associated facility of the hydropower project and determined that measures would be required to ensure the outcomes of the interconnection project consistent with the Performance Standards. This is in compliance with Performance Standard 1 (para. 5).</p> | <p>IFC agrees that the IP was an associated facility, subject to the PS requirement for the client to “address those risks and impacts [resulting from a third party’s actions] in a manner commensurate with the client’s control and influence over the third parties” (PS1, para 9).</p> | N/A |
| 2. | <p>IFC, in collaboration with the other lenders, negotiated a Direct Agreement which required UETCL to comply with the lenders’ environmental and social requirements, including IFC’s PSs. The Direct Agreement established a framework for supervision of the interconnection project in accordance with IFC’s Performance Standards. This is in compliance with the Sustainability Policy (paras. 17, 24 and 25).</p> | <p>The Direct Agreement captured UETCL’s commitment to the PSs, and included important reporting requirements regarding its land acquisition efforts. However, it did not establish the type of PS requirements applicable to an IFC direct investment, nor did it provide IFC the same remedies available to it as lender to a project. For instance, under this framework IFC could not request that information be provided or compliance be met as conditions of its disbursements to BEL. This is typical for associated facilities – a reality reflected in the PS language limiting application (as quoted above in response 1). IFC supported BEL to influence the process, and, alongside other Lenders, worked closely with AfDB, which did have a direct financial involvement with the IP. AfDB applied its institutional resettlement</p> | N/A |

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| | | standards, which were aligned with PS expectations. | |
| 3. | IFC did not have assurance that the RAPs provided for compensation for land and other assets at full replacement cost. This is not in compliance with PS5 (paras. 8 and 23). | <p>Land acquisition and resettlement is nearly always a complex process. The IP case was no exception, and was in fact further complicated by varying official compensation rates, unexpected high inflation levels, and unprecedented levels of speculation.</p> <p>Based on the original review by the resettlement expert preparing the RAP and subsequent discussions with the RAP implementation team, IFC believes that full replacement cost for land was generally achieved, as UETCL took responsibility for obtaining titles, and the RAPs accounted for market value plus transaction costs and depreciation, which taken together constitute full replacement cost. IFC and other Lenders were very attentive to the need for the RAP to meet the full replacement cost requirement. For example, Lenders raised concerns about whether local valuation rates included income lost in planting and re-growing trees. As a result, the 2008 RAP did explicitly confirm that local valuation rates were sufficient to cover this lost income.</p> | IFC is in the process of updating its resettlement good practice guidance. This guidance will include a recommendation for requesting an asset value update if the time lapse between the completion of the asset survey and the payment of compensation is significant. |

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| | | <p>However, we do acknowledge that payments occurred during a period of high inflation, which was not fully accounted for in the final valuation.</p> <p>We also appreciate the challenge of appropriately valuing legitimate ownership or use of assets against a backdrop of extreme speculation. Many individuals who did not previously own or occupy land in the IP corridor bought, rented, or licensed land that would subsequently have to be acquired by UETCL, such that 45% of the parcels to be acquired for the IP were within an 11-km stretch of the Kawanda line (i.e., 15% of its length, 11% of the overall length of the IP), which was located within the Mukono district (now split into Mukono and Buikwe Districts). In some cases, the land acquired were plots as small as 2m by 2m, deemed too small for economic exploitation.</p> <p>Surveyors also noted many high-value crops not found outside the IP corridor, often planted in unusually high densities and seemingly immediately prior to the survey. Speculation along the transmission line may have been influenced by the fact that the original crop rates set by district land boards adjacent to Mukono's differed in certain respects, especially for young</p> | |

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| | | <p>crops (which were ascribed higher values in Mukono than elsewhere).</p> <p>IFC generally regards UETCL efforts to de-incentivize speculation – such as compensating crops by area rather than individual plants, not compensating for young plants, and aligning compensation rates across the entire corridor – as aimed at aligning payments with market value while ensuring fairness across affected people, rather than undermining compliance with IFC’s PS requirements.</p> | |
| 4. | <p>There is no indication that IFC assured itself, once the compensation rates were finalized along with the 2008 RAP, that disclosure and meaningful consultation with affected people took place. This is not in compliance with PS5 (para. 9).</p> | <p>IFC disclosed the 2006 RAP, which was prepared by BEL, as part of its initial project disclosure. This followed IFC’s disclosure practice for direct investments at the time. As an associated facility, UETCL was not subject to the same disclosure requirements as a direct investment.</p> <p>It is also important to note that compensation rates are not subject to consultation. IFC expects companies to disclose rates and to consult with affected people around the process and options for resettlement.</p> | <p>With the 2012 PS update, IFC’s policy now provides for ongoing, follow-up disclosure for its direct investments. This was previously done only on an occasional basis, and was not typical practice at the time of IFC’s investment in the Bujagali HPP.</p> |

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| 5. | <p>CAO finds that IFC did not assure itself that the RAP included an assessment of the capacity of the Chief Government Valuer and ultimately measures for the client to bridge the gap in capacity. This is not in compliance with the Sustainability Policy (para. 15) and PS5 (para. 22).</p> | <p>The Chief Government Valuer (CGV) is the Ugandan government authority (in the Land Valuation Division) responsible for determining compensation values. The CGV is usually involved at the level of setting principles and rates, although in this instance the CGV did become involved in some individual cases. The CGV was independent of the government entity carrying out the land acquisition and building the associated facility.</p> <p>Assessing the capacity of an independent government valuer falls beyond PS5 requirements, and private companies typically are not in a position to question a government-led process. Therefore, IFC does not expect private companies to control such a process, but instead requires them to address any discrepancy in the final outcomes relative to PS5 requirements. In this case, IFC believes that the outcomes were consistent with those of PS5.</p> | <p>IFC appreciates the particular challenges associated with government-led resettlement. To provide additional guidance to Specialists, the E&S department has recently developed an internal Good Practice Note on “Dealing with Government Managed Resettlement in Private Sector Projects.”</p> |
| 6. | <p>Although IFC relied on AfDB to take a leading role in relation to the supervision of resettlement activities under the interconnection project, IFC had in place reporting and other oversight structures as required to</p> | <p>IFC agrees that we sought diverse sources of information and leverage. It is important to consider that the IP was an associated facility and the supervision structure was not equivalent to a direct investment, and financial leverage was absent. Thus, IFC’s</p> | <p>N/A</p> |

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| | supervise resettlement activities associated with the interconnection project and to require compliance with the Performance Standards. This is in compliance with IFC's Sustainability Policy (para. 26), PS1 (para. 24), and the ESRP v2 (para. 6.1.1). | supervision of the IP was not underpinned by the same level of leverage as was AfDB's direct investment, hence our expectation that AfDB be in a lead role with respect to the IP, while supported by BEL's broader Lender group. | |
| 7. | CAO finds that despite IFC considering in November 2008 that land valuation and compensation problems had been solved, it soon became apparent that it was and remains questionable whether compensation at full replacement cost has been achieved. CAO finds that IFC failed to respond to this challenge in a way that would generate corrective actions. This is not in compliance with IFC's Sustainability Policy (para. 26) and PS5 (para. 20), as affected people were neither promptly compensated nor is it demonstrated that they were compensated at full replacement cost. | <p>IFC believes that evidence cited in CAO's report does support the notion that the Lenders were concerned throughout supervision with compensating affected people at market rates, which was the major component of full replacement cost. For example, a Lenders' mission learned in November 2009 that the CGV was using current market rates in considering revaluation of assets.</p> <p>We agree on the importance of ensuring compensation at full replacement cost, though we also acknowledge the challenges involved in this case. Over the course of the current Bujagali-07 investigation, the number of complainants has reportedly risen and has brought in possible complainants from districts other than Buikwe (formerly part of Mukono District, where young crops were ascribed a higher value). As indicated above, IFC agrees with CAO on the importance of follow-up to</p> | In its own consultation with affected people, IFC confirmed general satisfaction with the compensation rates. The majority of complaints raised in the Bujagali-07 case seem to have arisen as a result of the Bujagali-05 mediated settlement, which reopened compensation for those complainants and arrived at rates that seem to exceed market value. IFC understands that it may not be financially feasible (in this or any other case in Uganda) to apply the Bujagali-05 rates more broadly, but will engage with UETCL together with AfDB to i) identify and address any relevant gaps in existing IP-related reports reports vis-à-vis IFC and AfDB completion report requirements, and ii) close out any associated corrective actions. |

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| | | <p>confirm that key aspects of IFC and AfDB land acquisition and resettlement requirements were met. IFC will engage with UETCL together with AfDB to i) identify and address any relevant gaps in existing IP-related reports reports vis-à-vis IFC and AfDB completion report requirements, and ii) close out any associated corrective actions.</p> <p>Regarding timing, UETCL and BEL remained committed to compensating promptly, and the land acquisition proceeded apace with the construction of the transmission line. Compensation is often a lengthy process in a project with this many land transactions, and further delays arose in this case from people holding out on receiving compensation in hopes of securing higher rates.</p> <p>AfDB did, in its response to its own Independent Review Mechanism (IRM), acknowledge problems with the pace at which the compensation process was being carried out. AfDB noted a range of problems – not just with people seeking higher compensation, but also ownership disputes and speculative construction following the census of assets – that delayed the process. AfDB committed to working with UETCL to increase the</p> | |

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| | | capacity of UETCL’s resettlement implementation unit to address these issues. | |
| 8. | IFC did not have assurance that the grievance mechanism provided for under the RAP was sufficient to provide impartial recourse in case of disputes over the valuation of assets and crops. This is not in compliance with PS5 (para. 10). | IFC agrees that UETCL’s grievance mechanism in the IP project was not fit-for-purpose. | <p>The transmission line associated with this project has been completed. As such, making modifications to UETCL’s project-level grievance mechanism would not be helpful in response to this CAO finding. However, BEL remains an IFC direct investment and does have a fit-for-purpose grievance mechanism, which IFC reviews as part of supervision activities.</p> <p>Subsequent to this project, both IFC and CAO initiated work programs specifically on grievance mechanisms. IFC has published guidance, such as the Good Practice Note on “Addressing Grievances from Project-Affected Communities: Guidance for Projects and Companies on Designing Grievance Mechanisms” and is committed to appraise and supervise clients’ project-level grievance mechanisms. CAO has also developed an online “Grievance Mechanism Toolkit” to provide practical guidance for implementing grievance mechanisms</p> |

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| | | | in different sectors. IFC circulated information about CAO's Toolkit to its E&S Specialists and has encouraged uptake on this issue. |
| 9. | CAO notes that the exclusion of the interconnection project from the completion audit undermines IFC's ability to satisfy itself that the adverse socio-economic impacts experienced by the land acquisition and land-use restrictions related to the transmission line were mitigated and livelihood was, at a minimum, restored. This is not in compliance with IFC's Sustainability Policy (para. 26) and PS5 (para. 12). | IFC agrees on the general usefulness of completion audits. Consistent with IFC's leverage and influence over our direct investment client, IFC requested and received a completion audit from BEL for the hydropower plant site. As mentioned above, IFC had only indirect leverage over UETCL in relation to the IP, given it was an associated facility. In this case, BEL did request and receive an interim completion audit for the IP, based on the requirement of the Direct Agreement. UETCL also submitted a project completion report to AfDB in 2016, which included coverage of land acquisition and compensation. | IFC shares CAO's concerns about mitigating impacts and restoring livelihoods. As described above in response 7, further work on this aspect will be undertaken in collaboration with AfDB and UETCL. |
| 10. | CAO finds that significant numbers of households whose land was acquired for the transmission line likely did not receive compensation at full replacement cost. Hence, CAO finds that IFC did not assure itself that its investment was carried out in a manner that appropriately compensated households impacted by land | We note efforts made on the part of all BEL's Lenders, and AfDB in particular as lender to both BEL and the IP, to ensure that UETCL provided the land titling (the major transaction cost associated with the land acquisition) and that compensation followed market value. IFC believes that full replacement cost was achieved, with the possible exception of an inflation adjustment (noting that this impact would | Follow-on actions have been outlined above in response 7. |

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| | <p>acquisition. This is not in compliance with IFC's Sustainability Policy (para. 8).</p> | <p>have been partially, but not fully, mitigated by the payment of a disturbance allowance).</p> <p>The Bujagali-05 settlement included rates seemingly above fair market value. Nevertheless, we acknowledge the importance of ensuring that the threshold of 'full replacement cost' was met. This issue will be covered by the supplemental actions already described above.</p> | |