



CAO ASSESSMENT REPORT

**Regarding Complaint in Relation to
IFC's Indorama Kokand, Hamkor Equity/SL, Hamkorbank RIs, Hamkorbank SL, GTFP
Hamkor, Projects (#38266, 27615, 30893, 32024, 35062, 36170, 33596, 30657)**

March 2018

*Office of the Compliance Advisor Ombudsman
for the International Finance Corporation and
Multilateral Investment Guarantee Agency*
www.cao-ombudsman.org

About CAO

The Office of the Compliance Advisor Ombudsman (CAO) is the independent accountability mechanism for the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA), members of the World Bank Group. CAO reports directly to the President of the World Bank Group, and its mandate is to assist in addressing complaints from people affected by IFC/MIGA-supported projects in a manner that is fair, objective, and constructive, and to enhance the social and environmental outcomes of those projects.

For more information, see <http://www.cao-ombudsman.org/>

TABLE OF CONTENTS

- LIST OF ACRONYMS 4
- 1. OVERVIEW 5
- 2. BACKGROUND 5
 - 2.1. The Projects 5
 - 2.1.1. IFC’s project with IKT 5
 - 2.1.2. IFC’s projects with Hamkorbank..... 5
 - 2.2. The Complaint 6
- 3. ASSESSMENT SUMMARY 6
 - 3.1. Assessment method 7
 - 3.2. Summary of issues..... 8
 - 3.2.1. Complainants’ Perspective 8
 - 3.2.2. IFC Clients’ Perspective..... 9
 - 3.3. Agenda for Dialogue 10
- 4. NEXT STEPS..... 11
- ANNEX A. CAO COMPLAINTS HANDLING PROCESS..... 12

LIST OF ACRONYMS

CAO	Office of the Compliance Advisor Ombudsman
ESAP	Environmental and Social Action Plan
GTFP	Global Trade Finance Program
IFC	International Finance Corporation
IKT	Indorama Kokand Textile
ILO	International Labour Organization
ILRF	International Labor Rights Forum
MIGA	Multilateral Investment Guarantee Agency
MSME	Micro, Small, and Medium Enterprises
NGO	Non-governmental organization
UGF	Uzbek-German Forum for Human Rights

1. OVERVIEW

In June 2016, CAO received a complaint related to several International Finance Corporation (IFC) projects in Uzbekistan. CAO found the complaint eligible for further assessment in August 2016 in relation to two IFC clients: Indorama Kokand Textile (IKT), a cotton yarn producer that received financing from IFC to expand its textile plant; and Hamkorbank, a licensed commercial bank headquartered in Andijan, Uzbekistan, with which IFC has seven active projects. The complaint was filed by a coalition of non-governmental organizations (NGOs) on behalf of Uzbek human rights monitors and alleged victims of forced labor in the cotton fields (the “Complainants”). The complaint raises concerns about the existence of forced labor in IKT’s supply chain. In regards to Hamkorbank, the complainants state that there is significant risk that Hamkorbank participates in a “coercive financial system and is not conducting adequate due diligence to ensure its participation is not supporting forced labor and the related attacks against independent labor monitors.” The complaint also states that IFC’s investment in Hamkorbank may finance companies that utilize or benefit from forced labor in the cotton system, and that IFC has not fulfilled its due diligence and supervision responsibilities. CAO found the complaint eligible in August 2016 and began an assessment of the issues raised in the complaint. During the assessment, the Complainants and the IFC clients agreed to engage in a voluntary dispute-resolution process facilitated by CAO. This Assessment Report provides an overview of the assessment process, including a description of the project, the complaint, the assessment methodology, and next steps.

2. BACKGROUND

2.1. The Projects

2.1.1. *IFC’s project with IKT*

IFC has an active project with IKT, a cotton yarn producer, to finance the expansion of a textile plant in the Fergana Valley, Uzbekistan.

IFC’s investment is a senior A Loan up to US\$40 million to IKT. According to IFC disclosures, the purpose of the investment is to allow IKT to further expand its capacity in Uzbekistan, leading to increased exports of local cotton yarn and availability of good quality raw material for the local weaving and knitting industry, thus enhancing the growth of the local textile industry and increasing industrial employment.

Upon project completion, IFC indicates that IKT will become Uzbekistan’s third largest domestic consumer of cotton, increasing its current annual ginned cotton consumption of 38,000 tons to 50,000 tons per year. As a result, IKT will consume five percent of the country’s one million tons of total annual ginned cotton production.

The project was approved by the Board on December 17, 2015, and disbursement of the full amount took place on May 17, 2016.

2.1.2. *IFC’s projects with Hamkorbank*

IFC has seven active projects with Hamkorbank – a combination of equity and loan investments, as well as a Global Trade Finance Program (GTFP).

According to IFC disclosures, Hamkorbank was originally formed as a regional bank in the Fergana Valley, and has been transformed into a nationwide financial institution offering small

and medium enterprise (SME) loans, micro loans, consumer loans, and leasing products. Its shares are traded on the Tashkent stock exchange. The equity investment aims at broadening Hamkorbank's funding base and will be used for expansion of its financing of micro and small entrepreneurs in Uzbekistan. It also aims at supporting the Hamkorbank's strategy and assisting in its expansion.

IFC indicates that its loans aim to enable Hamkorbank to expand the scope of its lending program to micro, small, and medium enterprises (MSMEs), with a focus on remote areas, which is aligned with IFC's financial markets strategy for Uzbekistan. Finally, IFC's Global Trade Finance Program (GTFP) supports selected Hamkorbank export/import transactions.

2.2. The Complaint¹

The complaint to CAO was filed by the International Labor Rights Forum (ILRF), the Uzbek-German Forum for Human Rights (UGF), Human Rights Watch, and the Cotton Campaign, acting on behalf of four Complainants: three Uzbek human rights defenders, whose work focuses on combatting the risk of forced labor and child labor during the cotton harvest; and one laborer, who reports being forced to pick cotton on multiple occasions. Six other Uzbek human rights activists asked to add their names formally to the complaint during the assessment phase, bringing the total to ten. The nine complainants who did not request confidentiality requested CAO to disclose their names:

1. Elena Urlaeva, Human Rights Alliance of Uzbekistan, from Tashkent;
2. Dmitry Tikhonov, an Uzbek human rights defender in exile;
3. Uktam Paradaev², a human rights defender from Jizzakh;
4. Utkir Paradaev, a volunteer from Jizzakh who assisted in monitoring the cotton harvest;
5. Azimbay Ataniyazov, a human rights defender from Nukus, Karakalpakstan Autonomous Republic;
6. Malokhat Eshonkulova, a human rights defender and journalist from Samarkand;
7. Arysylanbay Oteпов, a human rights defender from Nukus, Karakalpakstan Autonomous Republic;
8. Haitbay Yakubov, "Najot" (Salvation) human rights organization from Khiva; and
9. Surat Ikramov, chairman of the Initiative Group of Independent Human Rights Defenders of Uzbekistan, from Tashkent.

3. ASSESSMENT SUMMARY

The purpose of a CAO assessment is to clarify the issues and concerns raised by the complainants, to gather information on how other relevant stakeholders see the situation, and to determine which process—dispute resolution or compliance—the complainants and the IFC clients would like to initiate to address the complaint. CAO does not gather information during assessment to make a judgment on the merits of the complaint.

¹ For the complete 21-page complaint letter, please see http://www.cao-ombudsman.org/publications/documents/Cao_submission_public_version.pdf

² Uktam Paradaev is an original complainant who initially requested CAO to keep his identity confidential and subsequently granted permission to publicly release his name.

3.1. Assessment method

CAO's assessment of the complaint consisted of:

- bilateral and confidential meetings with the Complainants;
- meetings with 17 other Uzbek human rights defenders, civil servants, and cotton pickers, who were referred to CAO by the complainants and NGOs supporting the complaint;
- meetings with representatives of the NGOs supporting the Complainants;
- a desk review of IFC's project documentation and meetings with IFC's project teams for IKT and Hamkorbank;
- meetings with World Bank representatives in Tashkent and Washington, DC;
- a visit to IKT's textile plant in Kokand, as well as meetings over the phone and in person in Tashkent with IKT management;
- two visits to Hamkorbank headquarters in Andijan;
- meetings with Mrs. Tanzila Narbaeva, Deputy Prime Minister and Chair, Coordination Council on Child and Forced Labor Issues in the Republic of Uzbekistan, and Mr. Aziz Abdulkakharovich Abdulkhakimov, Minister of Labor;
- meetings with representatives of Uzpakhtasanoatexport, Uzbekyengilsanoat and the Chamber of Commerce and Industry of Uzbekistan;
- meetings with representatives of regional government (hokimiyats) in Fergana and Bukhara;
- meetings with the leadership of the Federation of Trade Unions of Uzbekistan;
- a tour of the Jondor gin and a meeting with a farmer in the Fergana region;
- meetings with representatives of the International Labour Organization (ILO) in Tashkent;
- a meeting with a representative of the US Embassy in Tashkent;
- phone calls with the German Investment and Development Corporation (DEG) and the Netherlands Development Finance Company (FMO) project teams who also have projects with Hamkorbank; and
- phone calls with the IFC Advisory Services team working on the Sustainable Cotton Supply Chain Development project.

CAO was unable to contact one of the original four Complainants, and continues efforts to reach that individual, who requested their identity be kept confidential.

CAO extended the assessment period for this case, primarily due to the extra precautions needed to protect the identities and confidentiality of Complainants and others who wanted to speak with CAO, as well as related communications challenges. Complainants also needed sufficient time to understand CAO's mandate and procedures to make an informed decision as to how they wanted to proceed.

3.2. Summary of issues

This section summarizes the perspectives held by various stakeholders relevant to the assessment process.

3.2.1. Complainants' Perspective

In meetings with CAO, the Complainants largely reiterated the issues raised in the original complaint and provided additional details and updates from the 2016 and 2017 cotton planting, weeding, pruning, soil tilling, and harvesting seasons.

Some human rights defenders report that they and their family members have been threatened or physically abused because of their activism and monitoring work related to forced labor in the cotton sector. Some of these events are documented in the original complaint and complainants informed CAO that events that occurred during CAO's assessment were also because of their activism and monitoring activities. Elena Urlaeva reported that she was involuntarily committed to a psychiatric hospital in Tashkent on March 1, 2017, during CAO's first mission to Uzbekistan, and held there until March 23, 2017. In September 2017, Urlaeva and Malokhat Eshonkulova reported being detained by local police and government officials in Yaipan village in Uzbekistan District, Fergana Region and having their mobile phones, notepads, and a camera confiscated. In early October 2017, Urlaeva reported being detained and questioned for two hours by local police and the local Department of Internal Affairs in Kuk-Aral village, Buga District, and subsequently released. Urlaeva and Eshonkulova reported being detained again on October 15, 2017, by local police in Juma city in Pstdargam District, and having their digital records and notes destroyed.

The original complaint also states that Dmitry Tikhonov fled Uzbekistan after suffering reprisals and intimidation for his human rights work related to the cotton sector. The Complainants expressed their desire for Dmitry, who is currently living in exile, to be able to return safely to Uzbekistan.

Uktam and Utkir Pardaev informed CAO that they believe their previous arrests and convictions on unrelated charges were actually intended to stop them from conducting their cotton-related monitoring work. According to Uktam, in November and December 2015 he suffered beatings and was given less than the standard prisoner rations of food and water while in jail. He says he is still under probation until 2019 and has to register with the Jizzakh City Department of Internal Affairs twice a month.

As noted in the original complaint letter, the Complainants also state that IFC has not fulfilled its due diligence responsibilities in its IKT investment with regards to child and forced labor in the cotton supply chain. They also say there is no evidence that IKT will meet the requirements of IFC's Performance Standard 2 (PS2) on Labor and Working Conditions within a reasonable time, or at all, citing PS2 paragraphs 27 and 29 specifically.

As mentioned above, CAO met with several other Uzbek human rights defenders, cotton pickers, and alleged victims beyond the eight formal Complainants. For the government

employees who refuse to pick cotton, they informed CAO that they have to pay for substitute pickers or they are otherwise threatened with job loss, and/or loss of public services like water, gas, and electricity. University students report being threatened with expulsion or receiving lower grades. Others who refuse to pick cotton and/or try to gather evidence of forced labor reported being detained and threatened by police or security services and having their family members threatened.

Some individuals reported to CAO that they and/or their family members voluntarily pick cotton for the extra income. These individuals' concerns centered more around the need to improve inadequate or dangerous working conditions for cotton pickers.

The Complainants further noted that since the election of President Mirzyoyev, the overall political situation in Uzbekistan is changing and evolving. The Complainants initially requested a compliance review of IFC's loans to IKT and loan and equity investment in Hamkorbank in the original complaint letter. However, during the assessment, the Complainants, with the exception of Malokhat Eshonkulova, informed CAO of their preference to initiate a dialogue with Hamkorbank and IKT through CAO's Dispute Resolution function to try to resolve the complaint issues. Complainants also noted their desire to meet with IFC under the auspices of CAO's Dispute Resolution function to better understand IFC's due diligence and project supervision, as well as to request IFC assistance in addressing the complaint issues. Malokhat Eshonkulova informed CAO that she did not support the dialogue process and preferred that CAO's Compliance function conduct an appraisal of the complaint.

3.2.2. IFC Clients' Perspective

IKT

IKT explained to CAO that to comply with IFC's Performance Standards, they took measures to reduce the risk that IKT would source cotton that is harvested through forced labor or child labor. One of IKT's first commitments was to procure cotton exclusively from areas which are part of ILO's annual third-party monitoring of World Bank-financed projects in the agriculture, water, and education sectors in Uzbekistan.³ Later, IFC also designed a risk index, which identifies districts where they believe the risk of forced labor and child labor is higher – referred to as “red” districts. IKT commits not to source cotton from those red districts.

According to IKT, it claims it can trace the cotton it buys back to the gins where it is processed, because each individual cotton bale is labeled with a number that corresponds to the gin it comes from. Each gin sources cotton from specific districts, which allows one to avoid sourcing cotton from any forbidden districts. IKT has installed signs inside their premises to remind all personnel of the forbidden gin numbers, which correspond to the forbidden districts.

IKT also developed a policy on forced labor and child labor, a copy of which was provided to CAO. Furthermore, IKT informed CAO that they are open to speak with anyone who has evidence of forced or child labor in IKT's supply chain, so that appropriate actions can be taken. IKT states that it conducts periodic third party human resources audits at its facilities to verify compliance to international standards.

IKT indicated that it regularly shares its business practices with other local firms at periodic business forums organized by the government – notably Corporate Social Responsibility practices and best manufacturing practices – to ensure production of high-quality cotton yarn.

³ For more information on the ILO third-party monitoring, please see http://www.ilo.org/ipec/Informationresources/WCMS_543130/lang--en/index.htm

Their aim is to participate in raising the general quality and reputation of Uzbek cotton. They also believe that, with the assistance of the World Bank and ILO, any current issues with respect to forced labor in Uzbekistan can be addressed.

Hamkorbank

Hamkorbank states that it has an Environmental and Social Management System (ESMS) and conducts monitoring of medium risk clients once a year, and high-risk clients twice a year, to ensure compliance. Hamkorbank also informed CAO that, in 2017, their Executive Board sent a letter, a copy of which was provided to CAO, to all its branches that emphasized the prohibition of forced labor of branch employees to harvest cotton and noted that strong disciplinary measures would be taken against branch managers where evidence of forced labor of Hamkorbank employees is identified. Hamkorbank notified CAO that it sent out notification letters urging its clients to restrict purchase of cotton from the red districts identified by IFC, and in turn clients have responded that they will support and comply with Hamkorbank's recommendation.

Hamkorbank finances agricultural farmers whose main business activity is farming and agriculture. Some of these farmers may have a small portion of land on which they grow cotton. However, Hamkorbank claims that when it conducts periodic monitoring, it ensures that the financing provided is not used for cotton. According to Hamkorbank, agricultural farmers' portion of their loan portfolio is 0.15 percent, while 7 percent of the loan portfolio is comprised of textile companies.

Generally, Hamkorbank indicates that it expects positive changes in the cotton sector, pointing out the existence of new government decrees and the ministerial and presidential portals created to lodge complaints. Hamkorbank also believes that the current government plans to diversify agricultural land and mechanize the cotton harvest will also lead to positive change.

Hamkorbank is open to dialogue with the Complainants under the auspices of CAO's Dispute Resolution function. They also expressed interest in possibly inviting their clients involved in the cotton and textile industries to participate in the dialogue at the appropriate time.

3.3. Agenda for Dialogue

During meetings with CAO, stakeholders articulated their respective key goals and interests, many of which were shared by all parties. It may be beyond the ability and mandate of CAO to help local stakeholders achieve their broader goals. Nonetheless, these goals can provide some common ground to improve understanding and assist local parties in developing mutually beneficial options to resolve the complaint. The following is a summary of the stakeholders' key goals and interests as heard and understood by the CAO team:

- eliminate the risk of child and forced labor in Uzbekistan's cotton sector;
- support sustainable economic development in Uzbekistan;
- encourage constructive engagement among the Government of Uzbekistan, IFC, IFC clients, and civil society and human rights organizations, to discuss topics of mutual concern;
- apply and implement relevant IFC Environmental and Social Performance Standards in IFC projects; and
- work together on achieving the aforementioned goals to improve economic opportunity and Uzbekistan's international image and reputation.

Based on the views of the relevant stakeholders, the primary questions that would need to be answered through CAO's Dispute Resolution function are:

1. How can relevant parties work together to demonstrate and ensure that there is no forced labor in IFC's IKT and Hamkorbank projects and related supply chains?
2. Focusing on IKT's supply chain and Hamkorbank's Environmental and Social Management System, how might inadequate working conditions for cotton field workers be identified, improved, and monitored?
3. How might relevant parties contribute to a broader discussion about how to improve cotton-related monitoring for potential forced labor and child labor?

During the assessment, complaint signatories discussed the possibility of inviting additional human rights activists and forced labor victims to participate in the dispute resolution process.

Many stakeholders also offered various ideas and suggestions for how to address the complaint issues and improve the overall cotton sector in Uzbekistan. As part of the dispute-resolution process, CAO looks forward to working with the parties to help them engage in constructive dialogue, share their ideas and proposals with one another, and develop mutually beneficial options to resolve the complaint.

4. NEXT STEPS

The Complainants (with the exception of Malokhat Eshonkulova), IKT, and Hamkorbank have agreed to engage in a voluntary dialogue process convened by CAO's Dispute Resolution function. CAO will facilitate this process, including assisting the parties to prepare for dialogue, agreeing on ground rules, and working together in a collaborative way to try and reach resolution of the issues as raised in the complaint and summarized in this assessment report. Depending on the results of the Dispute Resolution process, CAO may also need to consult with Malokhat to determine how to handle any outstanding issues.

ANNEX A. CAO COMPLAINTS HANDLING PROCESS

The Office of the Compliance Advisor Ombudsman (CAO) is the independent accountability mechanism for the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA), members of the World Bank Group. CAO reports directly to the President of the World Bank Group, and its mandate is to assist in addressing complaints from people affected by IFC/MIGA-supported projects in a manner that is fair, objective, and constructive, and to enhance the environmental and social outcomes of those projects.

The initial assessment is conducted by CAO's Dispute Resolution function. The purpose of CAO's assessment is to: (1) clarify the issues and concerns raised by the complainant(s); (2) gather information on how other stakeholders see the situation; and (3) help stakeholders understand the recourse options available to them and determine whether they would like to pursue a collaborative solution through CAO's Dispute Resolution function, or whether the case should be reviewed by CAO's Compliance function.

This document is a preliminary record of the views heard by the CAO team, and explanations of next steps depending on whether the parties choose to pursue a Dispute Resolution Compliance process. This report does not make any judgment on the merits of the complaint.

As per CAO's Operational Guidelines,⁴ the following steps are typically followed in response to a complaint that is received:

Step 1: **Acknowledgement** of receipt of the complaint

Step 2: **Eligibility:** Determination of the complaint's eligibility for assessment under the mandate of the CAO (no more than 15 working days).

Step 3: **Assessment:** Assessing the issues and providing support to stakeholders in understanding and determining whether they would like to pursue a consensual solution through a collaborative process convened by CAO's Dispute Resolution function, or whether the case should be handled by CAO's Compliance function to review IFC's/MIGA's environmental and social due diligence. The assessment time can take up to a maximum of 120 working days.

Step 4: **Facilitating settlement:** If the parties choose to pursue a collaborative process, CAO's Dispute Resolution function is initiated. The dispute-resolution process is typically based on or initiated by a Memorandum of Understanding and/or mutually agreed-upon ground rules between the parties. It may involve facilitation/mediation, joint fact finding, or other agreed resolution approaches leading to a settlement agreement or other mutually agreed and appropriate goal. The major objective of these types of problem-solving approaches is to address the issues raised in the complaint, and any other significant issues relevant to the complaint that were identified during the assessment or the dispute-resolution process, in a way that is acceptable to the parties affected.⁵

OR

⁴ For more details on the role and work of CAO, please refer to the full Operational Guidelines: http://www.cao-ombudsman.org/documents/CAOOperationalGuidelines_2013.pdf

⁵ Where stakeholders are unable to resolve the issues through a collaborative process within an agreed time frame, CAO Dispute Resolution will first seek to assist the stakeholders in breaking through impasse(s). If this is not possible, the Dispute Resolution team will inform the stakeholders, including IFC/MIGA staff, the President and Board of the World Bank Group, and the public, that CAO Dispute Resolution has closed the complaint and transferred it to CAO Compliance for appraisal.

Compliance Appraisal/Investigation: If the parties opt for a Compliance process, CAO's Compliance function will initiate an appraisal of IFC's/MIGA's environmental and social due diligence of the project in question to determine whether a compliance investigation of IFC's/MIGA's performance related to the project is merited. The appraisal time can take up to a maximum of 45 working days. If an investigation is found to be merited, CAO Compliance will conduct an in-depth investigation into IFC's/MIGA's performance. An investigation report with any identified non-compliances will be made public, along with IFC's/MIGA's response.

Step 5: **Monitoring and Follow-up**

Step 6: **Conclusion/Case closure**