Compliance Appraisal of a Complaint Regarding IFC’s Exposure to the Dairi Prima Mineral Mine in Indonesia Through an Investment in Postal Savings Bank of China
About CAO

The Office of the Compliance Advisor Ombudsman (CAO) is the independent accountability mechanism of the International Finance Corporation (IFC) and Multilateral Investment Guarantee Agency (MIGA), members of the World Bank Group. We work to facilitate the resolution of complaints from people affected by IFC and MIGA projects in a fair, objective, and constructive manner, enhance environmental and social project outcomes, and foster public accountability and learning at IFC and MIGA.

CAO is an independent office that reports directly to the IFC and MIGA Boards of Executive Directors. For more information, see www.cao-ombudsman.org.

About the Compliance Function

CAO’s compliance function reviews IFC and MIGA compliance with environmental and social policies, assesses related harm, and recommends remedial actions where appropriate.

CAO’s compliance function follows a three-step approach:

**Appraisal**
- Preliminary review to determine whether a complaint or internal request merits a compliance investigation.

**Investigation**
- Systematic and objective determination of whether IFC/MIGA complied with its environmental and social policies and whether there is harm related to any non-compliance.

**Monitoring**
- Verification of effective implementation of management actions developed in response to the findings and recommendations from a compliance investigation.
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Executive Summary

In 2015, IFC invested equity in Postal Savings Bank of China (PSBC), the fifth largest commercial bank in the People’s Republic of China. This compliance appraisal responds to a community complaint about Dairi Prima Mineral (DPM), a zinc and lead mine under development in North Sumatra, Indonesia. The complainants assert that IFC is exposed to the mine through its investment in PSBC. They allege that the potential failure of the mine’s planned tailings dam presents significant and potentially irreversible risks to people and the environment. Additional allegations include risks of water contamination from the mine’s planned tailings dam, inadequate stakeholder engagement and information disclosure, failure to recognize potentially affected communities as Indigenous Peoples, and risks to community safety and social cohesion.

As set out in this appraisal report, CAO has decided not to initiate a compliance investigation in response to this complaint. While the complaint meets the criteria for a compliance investigation, PSBC no longer has active loans with the mine’s majority owner or its parent company. In cases where IFC is no longer exposed to a project at the time of appraisal, the CAO Policy requires CAO to consider whether there would be particular value in terms of accountability, learning, or remedial action to initiate a compliance investigation despite the IFC exit. In this case, CAO concludes that there would be no such particular value in an investigation and has thus decided to close the case at appraisal.

Context and Investment

In December 2015, IFC made a US$286 million equity investment in Postal Savings Bank of China. The stated purpose of the investment was to help promote access to finance for China’s unbanked. The majority of PSBC’s borrowers are micro, small and medium sized enterprises and individuals, but the bank also has a portfolio of corporate lending to larger businesses. IFC’s initial investment equated to a 0.69 percent equity stake in PSBC, declining to an approximately 0.26 percent stake as of February 2022. Through its investment in PSBC, IFC became exposed to environmental and social risks related to PSBC’s lending activities and investments.

The Complaint and IFC Exposure

In October 2019, CAO received a complaint from two local residents on behalf of themselves and other community members living in the vicinity of the Dairi Prima Mineral project. DPM is a zinc and lead mine under development in the Dairi Regency of North Sumatra province, Indonesia.

The complaint argued that IFC was exposed to DPM through its investment in PSBC and another commercial bank. CAO found the complaint to be eligible in relation to PSBC only. At the time, PSBC had active working capital loans to China Nonferrous Metal Industry’s Foreign Engineering and Construction Co. (NFC) and its parent company, China Nonferrous Metal Mining (Group) Co. Ltd. (CNMC). NFC is the majority owner of DPM and responsible for the Engineering, Procurement and Construction (EPC) of the mine.

In their complaint and subsequent communication with CAO, the complainants allege that the DPM mine would adversely impact neighboring communities. Their specific concerns include:
a) **Risks related to the potential failure of the mine’s tailings dam**: The complainants allege that DPM’s design for the proposed tailings dam to store waste solids and water is inadequate for the site and could lead to a dam failure, with potential loss of life and impacts on livelihoods, land, and the environment.

b) **Risks of water contamination**: The complainants express concerns that the tailings dam’s operation could contaminate local water sources.

c) **Failure to adequately engage stakeholders and disclose project information**: The complainants claim that DPM has not properly consulted communities and that residents opposing the mine project have been threatened.

d) **Failure to recognize communities as Indigenous Peoples**: The complainants claim that most of the villagers surrounding the mine self-identify as Indigenous Peoples, but that DPM has not recognized them as such or consulted with them accordingly.

e) **Additional concerns**: These relate to the construction of an explosive storage facility near a settlement, causing community safety risks; air pollution risks related to the construction and operation of the mine; social risks related to in-migration of workers; and increased road traffic.

On February 11, 2022, CAO received separate responses to the complaint from IFC and PSBC. In summary, both IFC and PSBC contest the complainants’ view that IFC is exposed to the DPM mining project through its investments in PSBC. They assert that no financial links exist between PSBC and DPM. Their responses do not engage with the alleged harms associated with the planned mine raised by the complainants and outlined above.

**CAO Analysis**

Following the CAO Policy, the purpose of a CAO compliance appraisal is to determine whether a complaint merits investigation by applying the following criteria: a) whether there are preliminary indications of harm or potential harm; b) whether there are preliminary indications that IFC/MIGA may not have complied with its Environmental & Social (E&S) Policies; and c) whether the alleged harm is plausibly linked to the potential non-compliance.

Based on an initial review of available information, including responses from IFC Management and the client and available E&S information regarding the DPM project, CAO’s appraisal concludes that the complaint meets these three criteria, as summarized below:

**a) There are preliminary indications of harm to the complainants.**

- A preliminary review of available information suggests shortcomings in the design of DPM’s tailings dam and assessment of associated risks compared with good international industry practice for the construction of such facilities, particularly considering the topographical, geological, seismic and climatological characteristics of the site. In addition, available documentation includes design details of the tailings dam only for the first eight years of the mine’s projected 30-year life. These factors give rise to preliminary indications of risks of tailings dam failure, which could result in significant and potentially irreversible
impacts on the lives and livelihoods of several thousand villagers located downstream of the mine.

- Potential acidic drainage from the planned tailings dam also poses contamination risks to surface and groundwater sources that serve local communities. Based on a preliminary review of available information, there are indications that DPM’s plans to prevent, mitigate, and treat drainage may not be adequate, as described in this report.

- There are indications that the majority of potentially impacted communities self-identify as Indigenous Peoples, with their own language and communal traditional practices. A preliminary review of company information indicates that DPM has not recognized neighboring communities as Indigenous Peoples. As a result, the need for the mine to obtain Free, Prior and Informed Consent from affected Indigenous communities may have been overlooked.

- There is an onsite explosive storage facility built 50 meters from a settlement. Absent appropriate mitigation and safety measures there are indications of a risk to community safety in relation to this facility.

b) There are preliminary indications that IFC did not adequately review and supervise its investment in Postal Savings Bank of China in accordance with its environmental and social requirements.

In order to meet its Sustainability Policy commitments, IFC reviews and supervises the E&S risks and impacts of its investments. For a general-purpose investment in a financial intermediary (FI) such as PSBC, IFC reviews the E&S risk in the FI’s portfolio and its capacity to manage that risk in accordance with IFC’s Performance Standards. Depending on the level of risk, IFC sets E&S requirements for the FI to implement.

In this case, IFC appropriately categorized PSBC’s E&S risk as high. As a result, IFC required the bank to implement an E&S Management System to manage E&S risks in its investments and to apply IFC’s Performance Standards to all of its loans within 24 months. However, due to limitations on access to client information, IFC deferred a detailed diagnostic of PSBC’s E&S portfolio risk and systems until after making its investment. Accordingly, at the time of investment approval, IFC did not have a detailed understanding of the client’s E&S risk associated with lending activity or its capacity to manage that risk. As a result, it is not clear how IFC reached the conclusion that PSBC would be able to meet IFC’s E&S requirements “within a reasonable period” – a key threshold for IFC to move forward with an investment under the Sustainability Policy.

Following the Sustainability Policy, IFC is also responsible for monitoring how a banking client implements the E&S requirements set out in its investment agreements with IFC. In this case, IFC’s supervision consistently reported that PSBC had established an E&S Management System to assess and monitor risk in its investment portfolio.

However, several factors appear to contradict IFC’s stated confidence in PSBC’s capacity to apply IFC’s E&S requirements to its loans:

- PSBC’s E&S Management System does not refer to or require the application of the Performance Standards to its loans as required by its investment agreement with IFC.
• PSBC’s E&S Management System makes no reference to IFC’s Exclusion List and IFC does not appear to have commented on client financing of activities on IFC’s Exclusion List.

• A preliminary review of IFC supervision documentation does not indicate PSBC is applying the Performance Standards in pre-investment due diligence, legal agreements or supervision of its loans.

Taken together, these factors provide indications that IFC may not have complied with its obligation to supervise PSBC in line with both the IFC Sustainability Policy and the investment agreement between the two parties.

c) The alleged harms to the complainants are plausibly linked to potential non-compliance in IFC’s application of its environmental and social standards to PSBC.

The rationale for establishing a plausible link is as follows:

• IFC’s investment agreement required PSBC to apply the Performance Standards to “all financing operations.”
• PSBC provided financing to CNMC and NFC in the form of working capital loans.
• There are indications that IFC may not have supervised PSBC’s application of the Performance Standards to its financing operations in general, or its loans to NFC and CNMC in particular.
• NFC has effective control of DPM and is specifically responsible for the mine’s construction.
• The alleged harm to the complainants relates to issues covered by IFC’s Performance Standards.

IFC Exit and CAO Decision

When CAO finalized this compliance appraisal report in June 2022, IFC held an active investment in Postal Services Bank of China. However, PSBC reported during the appraisal process that it no longer had active loans with either CNMC or NFC. In circumstances where IFC has exited a project or sub-project by the time of a compliance appraisal, the CAO Policy requires consideration of whether an investigation would provide “particular value in terms of accountability, learning, or remedial action despite an IFC/MIGA exit.”

In this case, CAO considers that the lack of an ongoing financing relationship between PSBC and the DPM mine is likely to make remedial actions in response to any CAO finding or recommendation more challenging. Further, the indications of shortcomings in IFC’s application of its E&S requirements to PSBC outlined in this report are likely systemic in nature, with similar problems having been noted in CAO compliance reviews of other IFC banking investments. As a result, these issues may be more effectively addressed through other avenues, including as part of CAO’s ongoing compliance monitoring of IFC’s Financial Intermediaries portfolio.

Accordingly, although the complaint meets the criteria for a compliance investigation, considering that IFC no longer has a financial exposure to DPM through PSBC, CAO has decided to close
this case at appraisal. This appraisal report was published on the CAO website and shared with the Board, IFC Management, the client, and the complainants.
1. Introduction

This section provides an overview of IFC investment in the financial intermediary Postal Savings Bank of China (PSBC, “the client”), the complaint to CAO, and IFC’s link to the business activities in Indonesia that are the subject of the complaint.

a) Overview of IFC Investment

Postal Savings Bank of China is the fifth largest commercial bank in the People’s Republic of China, serving hundreds of millions of retail clients. The majority of borrowers are micro small and medium sized enterprises (MSMEs), and individuals, but the bank also has a portfolio of corporate lending to larger businesses.¹

In December 2015, IFC made an equity investment in PSBC with the stated purpose of helping to promote access to finance for China’s unbanked – some 235 million people, many of whom live in rural areas.²

The IFC invested US$286 million to acquire a 0.69 percent equity stake in PSBC. The investment was made as part of a PSBC offer to sell a 16.92 percent shareholding in a private placement of shares with strategic international and domestic investors ahead of listing on the stock exchange. IFC and PSBC also signed a Strategic Cooperation Agreement under which IFC provides expert advice to PSBC on MSME finance and rural finance, corporate governance, and E&S risk management.³

As of February 2022, IFC holds approximately 0.26% of shares in PSBC, which has a total market capitalization of approximately US$85 billion.⁴

b) Summary of Complaint

In October 2019, CAO received a complaint from two local residents on behalf of themselves and other community members living in the vicinity of Dairi Prima Mineral (DPM), a zinc and lead mining project under development in the Dairi Regency of North Sumatra province, Indonesia. This region is mountainous and prone to seismic activity, with a tropical rainforest climate including heavy rains from September to May.

The complaint argued that IFC is exposed to DPM through its investment in two banks, PSBC and Raiffeisen Bank International (RBI). The complainants received support from an international NGO, Inclusive Development International (IDI), and local partner organizations including Perhimpunan Bantuan Hukum dan Advokasi Rakyat Sumatera Utara (BAKUMSU).

At the time the complaint was submitted, exploratory activity and initial construction for the underground mine were underway.⁵ DPM also plans to build a processing factory near to the

¹ IFC Summary of Investment Information (SII), Project 35461, Postal Saving Bank of China
³ IFC Summary of Investment Information (SII), Project 35461, Postal Saving Bank of China
⁴ IFC Management Response to the CAO Complaint on PSBC Equity, February 11, 2022, para. iv.
mine, with an annual production capacity estimated at 1 million tons of zinc ore. The total concession size for the mine is 24,635 hectares. The mine is now under construction although work has slowed. Most of the mining infrastructure, including the tailings dam, has not yet been built.

The complainants allege that DPM will adversely impact neighboring communities. Their wide-ranging concerns include:

- **Risks of potential failure of the mine’s tailings dam**
  The complainants allege that the company has not conducted adequate safety assessments of the mine’s planned tailings dam. They assert that its design is inadequate for the extreme climate and seismicity of the site and inconsistent with good international industry practice as supported by their commissioned expert studies. Due to these alleged shortcomings, they express concerns over the risk of a potentially catastrophic failure of the tailings dam which would threaten lives, livelihoods, and the environment. The complainants state that 11 communities live around or downstream of the tailings dam and are largely reliant on farming for their livelihoods.

- **Risk of water contamination related to the tailings dam**
  The complainants express concern that operation of the tailings dam could lead to the contamination of surface and ground water used by local residents, with potential impacts on human health.

- **Failure to adequately engage stakeholders and disclose project information**
  The complainants claim that DPM has failed to adequately consult communities in the mine’s vicinity from early in the planning and exploration process. They allege that E&S information disclosure about the mine has been inadequate, particularly in regard to the tailings dam, design and safety features, and environmental impact assessments (EIAs). Community members also report receiving threats and allege that DPM and government officials are using tactics to divide communities.

- **Non-recognition of communities as Indigenous Peoples**
  The complainants claim that most of the villagers surrounding the mine self-identify as Indigenous Peoples, but that DPM has not identified them as such and has not consulted with them according to good international industry practice as applied to projects impacting Indigenous Peoples.

- **Other concerns**
  The complainants raise several other issues that are considered in this appraisal.
  
  o **Siting of an explosive storage facility**
  The original complaint refers to concerns over the use of protected forest area for infrastructure development generally. In communication with CAO, the complainants clarified that their concerns

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centered on DPM’s plan to build an explosive storage facility in a protected forest area, with potential impacts on the environment and water sources. During the appraisal, complainants informed CAO that the explosive storage facility was in fact built in another (non-forest) area, only 50 meters from homes. They expressed concerns over the risks to community safety associated with this close proximity to housing.

- **Air Pollution triggered by the mine operations**
  The complainants allege that, once operational, the mining site will cause air pollution that may lead to adverse health impacts for neighboring communities.

- **Social pressures and increased traffic**
  The complainants express concern about the negative social impacts of migrants from other provinces and countries entering their communities to work at the mine, as well as the increase in traffic due to in-migration and the mine’s construction and operation.\(^8\)

**c) IFC Exposure to the Dairi Prima Mineral Mine in Indonesia**

In March 2020, CAO determined the complaint eligible in relation to IFC’s investment in PSBC. At the time, PSBC had active working capital loans to China Nonferrous Metal Industry’s Foreign Engineering and Construction Co. (NFC) and its parent company, China Nonferrous Metal Mining (Group) Co. Ltd. (CNMC). NFC is the majority owner of Dairi Prima Mineral and the Engineering, Procurement and Construction (EPC) contractor for the mine. While the complainants asserted that PSBC was the underwriter for two CNMC bonds, CAO did not determine the complaint eligible on this basis as PSBC represented that it did not in fact underwrite the CNMC bonds.

CAO found the complaint ineligible in relation to IFC’s investment in Raiffeisen Bank International (RBI) as its alleged financial links to DPM’s minority owner, PT Bumi Resources Minerals were not considered to generate a material exposure. Figure 1 provides an overview of IFC’s exposure to DPM through PSBC, CNMC and NFC.

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During CAO’s assessment of the complaint, the parties failed to reach agreement to participate in a CAO supported dispute resolution process. In accordance with CAO Policy, the complaint was referred to CAO’s compliance function for appraisal in January 2022.

2. Compliance Appraisal’s Scope and Methodology

The scope of this compliance appraisal is limited to issues raised in the complaint (attached in Appendix A) and CAO’s Assessment Report. A CAO appraisal involves a preliminary review of available information. It does not lead to any definitive assessments or findings of harm or IFC/MIGA non-compliance. Applying the appraisal criteria and considerations set out in the CAO Policy, and discussed in detail in section 5 below, the CAO Director General may decide to initiate a compliance investigation of the complaint or close the case.

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10 CAO Policy, Sec. X, para. 88.
11 CAO Policy, Sec. X, para. 94.
12 CAO Policy, Sec. X, para 96-97.
This compliance appraisal was conducted by CAO staff with assistance from an external expert consultant to support the analysis of technical aspects of the complaint as they relate to indications of potential harm and potential non-compliance.13

CAO made the appraisal decision based on the appraisal criteria and other applicable considerations in the CAO Policy, taking into account the complaint, the assessment report, IFC’s Management Response to the complaint, and PSBC’s separate response and additional clarifications.

The appraisal process also considered:

- Additional documentation provided by the complainants;
- Available IFC and client documentation on the implementation of E&S requirements;
- Environmental impact statements related to the DPM mine;
- Media and publicly available documentation; and
- Satellite imaging.

CAO extends its appreciation to all parties mentioned in this report who have provided their perspectives, knowledge, and time.

3. Summary of IFC and Client Responses

The IFC and PSBC responses to the complaint provided to CAO are summarized below and attached in full as Appendix B and C. Both rejected the complainants’ premise that IFC is exposed to DPM’s mining site in Indonesia through its investment in PSBC.

a) IFC Response

IFC provided a Management Response to the complaint (“the Management Response,” see Appendix B). This contests the complainants’ view about financial links between Postal Savings Bank of China and Dairi Prima Mineral and does not address their specific concerns related to the DPM mine. To support its case that there is no link between PSBC and DPM, IFC presents the following arguments:

- PSBC confirmed that both CNMC and NFC did receive working capital loans from PSBC. However, IFC states that these working capital loans were subject to national legal and regulatory requirements which meant that it was not possible for CNMC or NFC to either use the proceeds of PSBC’s working capital loans to support a subsidiary or affiliate or to use the working capital loan proceeds to invest in an enterprise outside China such as the DPM mine.14
- IFC states that as a commercial bank established under the laws of People’s Republic of China, PSBC’s working capital loans are subject to China’s Law on Commercial Banks

13 The consultant was Dr. David Williams, Director of the Geotechnical Engineering Centre within the School of Civil Engineering at The University of Queensland and internationally recognized for his expertise in tailings dam design and management.
and the Interim Administrative Rules on Working Capital Loans, which restrict the use of such loans. Specifically, IFC points out that the proceeds of a working capital loan shall not be used by the borrower for fixed assets, equity, or capital investment in another enterprise.

Based on the above, IFC asserts that PSBC’s working capital loans to CNMC and NFC do not establish the alleged financial link between PSBC and DPM. As a result, IFC argues that PSBC cannot be expected to require DPM to apply IFC E&S requirements. In addition, IFC argues that alleged E&S risks or impacts related to the DPM project cannot be plausibly linked to PSBC or IFC or to any potential IFC non-compliance with E&S Policies. Thus, IFC states, the complaint does not satisfy the appraisal criteria for investigation following the CAO Policy.

**b) Client Response**

On February 11, 2022, CAO received a response from IFC’s client, PSBC, in relation to the complaint (see Appendix C). Neither the response nor the additional clarifications provided to CAO by PSBC address the concerns raised by community members about the E&S impacts of the DPM mine. PSBC states that it is not linked to DPM and that DPM is “far beyond its leverage”. The bank requests that CAO close the case, based on the arguments summarized below:

- PSBC clarifies that its connections with CNMC and NFC are only through working capital loans and notes the limitations on the use of working capital loans under Chinese law (as outlined in relation to IFC’s response above). PSBC further states that based on its inquiries, neither CNMC nor NFC used loans obtained from PSBC for the DPM mining project in Indonesia. As a result, PSBC asserts that there is no link between PSBC and DPM.

- PSBC argues that DPM does not fall within the definition of "Sub-Client" or "Sub-Project" under the CAO Policy, and IFC’s E&S standards do not apply to DPM. PSBC states that DPM is a fourth-tier subsidiary of CNMC and a third-tier subsidiary of NFC.

- PSBC refers to provisions of the IFC Financial Intermediaries (FI) Interpretation Note which state that an FI should apply the Performance Standards to project or long-term (over 36 months) corporate finance where the business activity includes higher E&S risks. In this case, PSBC argues that its working capital loans to CNMC and NFC are neither "project finance" nor "long-term (over 36 months) corporate finance", and do not involve "high-risk activities". Thus, PSBC asserts that there is no basis for applying the IFC Performance Standards to working capital loans in NFC and CNMC.

- For similar reasons, PSBC argues that there is no “direct linkage” between PSBC and DPM in relation to the complainants’ arguments and to international good practice standards on business and human rights.

Based on the above, PSBC concludes that the complaint does not meet the CAO Policy appraisal criteria in relation to preliminary indications of IFC non-compliance with its E&S Policies or plausible link between the alleged harm and the non-compliance.
4. **IFC Environmental and Social Policy Framework**

This section summarizes the 2012 Sustainability Framework requirements that apply whenever IFC makes an investment in a financial intermediary, such as PSBC. The IFC Sustainability Framework includes the Sustainability Policy (binding on IFC) and the Performance Standards (client requirements).

The Sustainability Policy states that IFC seeks to ensure that it carries out investment and advisory activities with the intent to “do no harm” to people and the environment. In order to achieve this, IFC conducts pre-investment review and supervision of its investments. IFC requires its clients to manage the E&S risks and impacts of their operations in accordance with the IFC Performance Standards.\(^\text{15}\) For a financial intermediary, this means implementing an Environmental & Social Management System (ESMS)\(^\text{16}\) to ensure that it applies the IFC Exclusion List and follows respective national law and requires higher risk business activities it supports to apply relevant requirements of the Performance Standards. The IFC Sustainability Policy does not differentiate between financial products (e.g., project, corporate or working capital finance) in terms of the requirement to apply the Performance Standards, but rather between the underlying E&S risks of the activity being financed.\(^\text{17}\)

The IFC Performance Standards (2012) define IFC clients’ responsibilities for managing the environmental and social risks and impacts of their business operations. Particularly relevant to the issues raised in this complaint are:

- **Performance Standard 1: Assessment and Management of Environmental and Social Risks and Impacts** sets requirements for integrated assessment of E&S risks, stakeholder engagement and disclosure, and management of E&S performance.
- **Performance Standard 3: Resource Efficiency and Pollution Prevention** sets requirements for efficient and effective resource use and pollution prevention in line with internationally disseminated technologies and practices.
- **Performance Standard 4: Community Health, Safety, and Security** sets requirements to avoid or minimize the risks and impacts to community health, safety, and security that may arise from project-related activities.
- **Performance Standard 6: Biodiversity Conservation and Sustainable Management of Living Natural Resources** sets requirements to protect and conserve biodiversity and maintain ecosystem services.

\(^\text{15}\) IFC Sustainability Policy 2012, para 7-9

\(^\text{16}\) An ESMS is a set of policies, procedures, tools and internal capacity to identify and manage a financial institution’s exposure to the environmental and social risks of its clients/investees. For further details on ESMS aspects, see IFC Performance Standard 1, IFC Interpretation Note for Financial Intermediaries (2018), and IFC’s First for Sustainability, available at [https://bit.ly/3qFLsc7](https://bit.ly/3qFLsc7).

\(^\text{17}\) As per IFC Sustainability Policy 2012, para. 35. FIs with portfolio and/or prospective business activities that present moderate to high environmental or social risks (i.e., Category FI-1 and FI-2) will require higher risk business activities they support to apply relevant requirements of the Performance Standards. Note also, IFC’s E&S Review Procedures (ESRP) in place at the time IFC made its investment in PSBC provided for IFC to treat working capital loans as a form of general corporate exposure and apply the Performance Standards to these loans (IFC ESRP 3.2.1, version 7).
- *Performance Standard 7: Indigenous Peoples* set requirements for the identification of Indigenous Peoples and to anticipate and avoid impacts of projects and seek their Free, Prior and Informed Consent in certain circumstances.

In addition, the Performance Standards require that mines be developed and managed in accordance with IFC Environmental, Health and Safety (EHS) Guidelines for Mining (2007).

### 5. Analysis

This section summarizes the analysis of the complaint, based on research, document review, and interviews conducted in January–May 2022. It presents analyses of the three appraisal criteria required to determine whether to initiate a compliance investigation. These criteria are:

- Whether there are preliminary indications of harm or potential harm;
- Whether there are preliminary indications that IFC/MIGA may not have complied with its E&S Policies; and
- Whether the alleged harm is plausibly linked to the potential non-compliance.

Finally, this appraisal analysis discusses an additional consideration outlined in the CAO Policy, namely whether an investigation would provide particular value in terms of accountability, learning, or remedial action despite an IFC/MIGA Exit.

#### a) Preliminary Indications of Harm or Potential Harm

A compliance appraisal must consider whether a complaint raises preliminary indications of harm or potential harm. CAO concludes that there are preliminary indications of potential harm on people and the environment in relation to the DPM mine in North Sumatra, Indonesia.

These are of particular concern in relation to the mine’s tailings dam. A preliminary review of available information suggests shortcomings in the design of the tailings dam and assessment of associated risks compared with good international industry practice for the construction of such facilities, particularly considering the topographical, geological, seismic and climatological characteristics of the site. These shortcomings give rise to significant risks to people and the environment associated with a potential failure of the tailings dam.

As a prelude to the discussion below, if the DPM mine was a direct IFC investment it would be a Category A project – the highest E&S risk level. Category A projects are defined as “business activities with potential significant adverse environmental or social risks and/or impacts that are diverse, irreversible, or unprecedented.” The DPM project fits this description given the potentially significant and irreversible E&S risks and impacts associated with the construction and operation of a large zinc mine and associated tailings dam.

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18 CAO Policy, para. 91.
19 IFC Sustainability Policy, para. 40.
Risks from potential failure of the mine’s tailings dam

Based on a preliminary review of available documentation, the planned DPM tailings dam presents clear indications of harm with risks of failure that could lead to significant adverse environmental or social impacts that are diverse, irreversible, or unprecedented.

As part of this compliance appraisal, CAO reviewed the 2021 addendum to DPM’s original Environmental Impact Assessment (EIA), conducted in 2005. This presents the most updated and comprehensive technical information available about the mine and the tailings dam design. While the EIA addendum references technical design documentation, it lacks details about tailings management and storage, with no details available beyond the first eight years of the projected 30-year mine life, which would be expected in an EIA following standard practice.

Tailings dams are used to store the fine-grained waste products from the processing of crushed and ground ores. DPM proposes to construct a tailings dam with an initial 25-meter-high starter dam to store the first eight years of tailings production. Available information suggests that the starter dam will be raised by placing fill on the downstream side of the dam though details about the design and the ultimate height of the dam are lacking.

Preliminary review of the documentation available indicates that DPM may not have employed good international industry risk management practices in assessing risks related to the climatic, geological and seismic conditions of the dam’s location, or the need to consider the dam’s design beyond the initial eight years of the mine’s projected 30-year life, particularly given the area’s seismic and climatological risks. These risks are elaborated further below.

First, the mine site is located in a region prone to earthquakes of strong magnitude and heavy rainfall, and its tailings dam would be located on a foundation of alluvium and volcanic ash (known as tuff). DPM identified these risk factors in its 2021 EIA addendum. The company acknowledged natural disaster risks in the mine site’s vicinity due to Indonesia’s location at the boundaries of three major plates, a high degree of topographic relief, and the highly porous and

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20 E&S information from DPM available in CAO’s files: DPM (2005), Environmental Impact Assessment; Revised Addendum to the EIA, 2019; Revised Addendum to the EIA, 2021 (all in Bahasa Indonesian). The 2021 Addendum (section 2.5.3) presents a new location for the tailings dam compared to what the 2005 EIA envisaged. The dam is relocated +/- 2km to the north of the processing plant in a non-forest area. CAO did not have access to technical studies that may have been commissioned by DPM.

21 DPM, Addendum to EIA, 2021, section 2.5.3. No details are given beyond the initial 25m-high starter dam to store the first eight years of tailings production.


23 This area is one of the world’s highest earthquake zones, near the Sumatra subduction megathrust which in 2004 and 2005 produced earthquakes of very high magnitude. https://bit.ly/3NFIPJs; https://on.doi.gov/3x2DyNn

weak nature of the tuff, which provides a poor foundation for the dam, with subsequent potential for saturation by rainfall and for landslides.\textsuperscript{25} Government documentation confirms these risks.\textsuperscript{26}

Further, the dam design presented in the EIA addendum only includes the initial eight-year starter dam. While available documentation does not specify the ultimate dam height, the starter dam will need to be significantly increased in size to store the tailings produced over the 30-year expected lifespan of the mine.\textsuperscript{27} Dam stability for the initial eight-year starter dam would be more readily achieved than for the ultimate dam height.

Finally, the proposed deposition of tailings as a slurry makes them susceptible to earthquake-induced liquefaction or flow, providing little strength to resist dam instability, and potentially causing any tailings elevated above the dam to overtop it and flow downstream.

The site’s high earthquake risk, high rainfall, steep topography, and poor foundation conditions increase the risk of the tailings dam being susceptible to failure. The dam’s location upstream of several thousand villagers and their farmland means that a dam failure would have potentially significant and irreversible effects on people and the environment.\textsuperscript{28}

Given the combination of high seismic risk, high rainfall, the ultimate height of the proposed dam, and the downstream location of villages, a tailings dam failure at the DPM site would be considered “extreme” under the ANCOLD Guidelines on Tailings Dams.\textsuperscript{29} This would require under good international industry practice a tailings dam to be designed to withstand one in 10,000-year flood and earthquake loadings. However, for the North Sumatra site, DPM has provided limited design information for only a one in 200-year earthquake applied to the eight-year dam height.

There are other indications of divergence from good industry practice in the dam’s design. DPM’s 2021 EIA addendum lacks recommendations on dam monitoring either during operations or post-closure. Further, DPM has provided only limited details about the proposed cover over the tailings at closure, and its function, placement, and revegetation. Finally, contaminated water from the tailings dam will have to be managed post-closure, and the acidic drainage and any runoff likely treated in perpetuity. No consideration of these issues is included in DPM’s available documentation.

In its 2021 EIA addendum, DPM claims that it followed the 2012 ANCOLD Guidelines in designing its planned tailings dam. However, the company provides few or no details on key design aspects

\begin{itemize}
\item \textsuperscript{25} DPM 2021 addendum, section 2.5.4.
\item \textsuperscript{27} Available documentation includes the tailings production expected in the first eight years as well as for the full 30 year expected lifespan of the mine. However, the three-dimensional shape of the tailings dam is not given. Based on available documentation, the dam needed to store the tailings produced over the 30-year expected lifespan of the mine may be 75m or higher.
\item \textsuperscript{28} DPM’s environmental impact assessment considers five villages as potentially affected by the mine, with over 6,000 inhabitants total. DPM (2021), Addendum to EIA, April 2021, section 3.3. Complainants state that there are 11 villages around and downstream from the tailings dam. Inclusive Development International, Indonesia: Preventing the looming Dairi Prima Mineral mine disaster, at: https://bit.ly/3xiJgBl
\item \textsuperscript{29} See ANCOLD (2012, revised in 2019), \textit{Guidelines on Tailings Dams – Planning, Design, Construction, Operation and Closure}. Australian Committee on Large Dams.
\end{itemize}
that would be referenced in an EIA for a tailings dam assessment prepared following ANCOLD (2012) and/or the GISTM. Accordingly, the available design documentation for the mine’s tailings dam appears to fall short of good international industry practice.

**Risk of water contamination from the tailings dam**

Review of available information points to preliminary indications of potential harm to both surface and groundwater from the mine’s planned tailings dam.

IFC’s EHS Guidelines on Mining note risks of water contamination associated with tailings dams due to acidic leaching, among other factors. Seepage and spillway flows from tailings dams contain contaminants in the form of dissolved heavy metals and sediment, with the potential to pollute downstream waterways and groundwater, causing health and environmental effects.

A review of DPM’s 2021 addendum to its Environmental Impact Assessment highlights potential risks to surface and ground water from acidic drainage and sediment associated with the current plans. In particular:

- The sulfidic tailings are expected to generate acidic drainage with high concentrations of dissolved metals (particularly lead and zinc) to surface and groundwaters, requiring treatment prior to release to the Sopokomil River.
- DPM proposes to settle suspended solids and treat the acidic drainage and rainfall runoff in a sediment pond, without specifying which method will be used or adequately describing the treatments envisaged and assessing whether they would be appropriate and effective.
- The sediment pond’s capacity may be inadequate to handle the likely high suspended sediment loads and flow rates, and to provide the required retention time for settling suspended sediment and treating contaminated water.

Accordingly, while the EIA addendum recognizes the risks of acidic drainage, it does not appear to offer related prevention, mitigation, and treatment plans to avoid generating potential impacts on health and the environment in line with good international industry practice.

**Adequacy of stakeholder engagement and disclosure of project information**

There are preliminary indications of potential harm in relation to the lack of disclosure of information and the lack of informed consultations with communities potentially affected by the mine. These apparent community engagement shortcomings likely restricted the ability of potentially affected people to participate in the impact assessment and mitigation planning process in order to address the project’s significant potential risks and impacts.

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30 These would typically include breach risk and consequence assessments; geotechnical, seismic, hydrological, and hydrogeological investigations, materials testing, and analyses; dam stability over the course of the dam’s operation (no details are provided beyond Year 8); foundation improvement, bearing capacity and permeability; the upstream toe drain; thickening and deposition of the tailings; catchment and dam hydrology and spillway design; and tailings dam closure (in perpetuity).

The following factors raise concerns of inadequate disclosure and engagement and their implications:

- Stakeholder engagement since 2005 may not have included all impacted communities. As documented, DPM’s outreach has been limited to a small number of communities and consultations. For instance, for the 2005 EIA, only four villages appear to have been considered and consulted\(^{32}\), although NGOs identified at least 11 villages likely to be affected by the mine’s construction and operation.\(^{33}\) In a 2021 survey of seven villages by an independent researcher, community members reported not having been adequately informed of the mine’s potential impacts.\(^{34}\)

- Neither the 2005 EIA, nor the 2019 and 2021 addenda, are publicly available today, and DPM and government authorities have disclosed very little E&S or technical information on the tailings dam design and safety, despite repeated requests from community organizations.\(^{35}\)

- There is no documentation indicating that DPM, its owners, or government authorities, contradict the complainants’ claims on lack of disclosure and adequate stakeholder engagement.

**Recognition of impacted communities as Indigenous**

There are preliminary indications of potential harm associated with the lack of recognition of potentially impacted communities as Indigenous Peoples and the resulting possibility that the need for Free, Prior, and Informed Consent from Indigenous communities may have been overlooked.

Recognition of community members as Indigenous would require the application of IFC’s Performance Standard 7 (Indigenous Peoples) to the project. This in turn would trigger higher standards of consultation and assessment, and potentially the requirement of Free, Prior and Informed Consent (FPIC), to ensure the mine is built and operates with due consideration of Indigenous Peoples’ practices and entitlements.

Preliminary indications that local communities may be Indigenous and DPM failed to recognize them as such include:

- Two main distinct ethnic or cultural groups live in the area, the Pak-Pak and the Batak Toba, in addition to smaller ethnic groups.
- DPM’s E&S information confirms that these are the main local ethnic groups but does not examine whether they should be considered Indigenous Peoples.\(^{36}\)

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\(^{35}\) Email exchange with complainants, April 2022.

\(^{36}\) As part of the 2021 addendum, a socio-economic and cultural study was conducted in five villages in the jurisdiction of Silima Pungga-pungga sub-district. Section 3.3., DPM (2021), Addendum to EIA, April 2021. On file.
• The company’s 2021 EIA addendum recognizes that these communities practise traditional communal production, distribution, and consumption systems, and have their own dialect and customary land and related traditions.\textsuperscript{37}
• Based on information from the complainants and other NGO sources, most villagers living around the mine appear to self-identify as Indigenous.\textsuperscript{38} Indonesia’s leading Indigenous Peoples organization likewise recognizes these communities as Indigenous.\textsuperscript{39}
• At national level, CAO notes the increasing recognition of Indigenous Peoples and their rights under Indonesian law and in practice.\textsuperscript{40}
• Based on the above information, these communities likely meet IFC’s definition of Indigenous Peoples.

Additional concerns about the mine’s construction and operation

Other indications of potential harm related to the community complaint include:

• An explosive storage facility, built on the site in 2020, is situated 50 meters from a settlement.\textsuperscript{41} Given its location, and the absence of information in available documentation that DPM has provided mitigating and safety measures, this facility presents a potential risk for the nearby community.\textsuperscript{42} There are thus preliminary indications of potential harm in relation to the explosive storage facility as currently located.

• There are environmental and health risks commonly associated with air pollution from mining and smelting, as well as increased road traffic and social risks stemming from the predicted influx of workers connected to the mine’s development and operation. CAO’s review of available documentation points to limited assessment and mitigation of these risks.\textsuperscript{43} Thus, while these risks have not materialized to date and can readily be mitigated, there is insufficient information from DPM to dismiss the complainants’ concerns.

b) Preliminary Indications of Non-compliance with IFC E&S Policies

A compliance appraisal must consider whether a complaint raises preliminary indications that IFC may not have complied with its E&S Policies. In this case, there are preliminary indications that

\textsuperscript{37} Section 3.3.3.1 Traditional Economic Systems and Section 3.3.3.4. Asset Ownership, DPM (2021), Addendum to EIA. On file.
\textsuperscript{38} In a recent household survey of 87 people in villages that may be affected by the mine, when asked if the respondent’s household was Indigenous, 95.3% of respondents said their household was Indigenous. Bakumsu, Report on the level of community Free, Prior and Informed Consent for the proposed DPM Mine, February 2022, in CAO files. And email exchange with complainants, Feb-May 2022.
\textsuperscript{40} UN Special Rapporteur on the right to food (2018), mission to Indonesia, A/HRC/40/56/Add.2. https://bit.ly/3asednd
\textsuperscript{43} For instance, DPM’s 2021 addendum includes forecasts on air quality decline due to construction and operation but offers insufficient information on mitigating measures. DPM 2021 addendum to the EIA.
IFC did not adequately review or supervise its investment in Postal Savings Bank of China in accordance with E&S requirements.

This section summarizes IFC’s pre-investment review of PSBC and investment supervision, before presenting a preliminary analysis of IFC’s compliance with relevant E&S Policy requirements.

**IFC pre-investment review**

When IFC makes a general-purpose investment in a financial intermediary (FI) such as PSBC, it conducts due diligence. This includes reviewing the FI’s portfolio and prospective business activities to identify whether it finances sub-projects with E&S risks. IFC also evaluates the FI’s Environmental & Social Management System (ESMS) and its capacity to manage E&S risks across its investment portfolio.

Based on this review, IFC categorizes the E&S risk of its investment and sets E&S requirements for the FI to implement. Under the Sustainability Policy, IFC’s E&S requirements for a financial intermediary such as PSBC include:

- Operating an ESMS that is commensurate with the level of E&S risk in its investment portfolio;
- Applying IFC’s Exclusion List and following respective national law; and
- Applying relevant IFC Performance Standards to higher risk business activities the FI supports.

Where an FI is not yet implementing an ESMS commensurate to risk or, as relevant, applying the Performance Standards prior to an IFC investment, IFC and the client agree to a time bound E&S Action Plan (ESAP) to achieve compliance with IFC’s E&S requirements.

IFC presents each proposed FI investment, including a summary of its pre-investment review and its proposed E&S requirements, to the IFC Board for approval. IFC can only finance investment activities that are expected to meet the requirements of the Performance Standards within a reasonable period. Upon IFC Board approval, IFC finalizes and commits to legal agreements with the FI that include relevant E&S requirements.

In this case, the scope of IFC’s pre-investment review was limited. PSBC sought to offer a select number of investors the opportunity to acquire equity via a pre-Initial Public Offering private placement. PSBC limited the scope of information to be provided to investors, including IFC. IFC received access to a data room to review client documentation, was permitted one day of meetings with client staff, and did not have access to the client’s loan files. It was therefore not possible for IFC to conduct its usual level of review in order to understand the underlying portfolio.

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44 IFC investments in a financial intermediary are categorized as FI-1 (high risk), FI-2 (medium risk) and FI-3 (low risk). See IFC Sustainability Policy (2012), para 40 for further details.
45 IFC Sustainability Policy 2012, para 35.
46 IFC Exclusion List for FIs lists activities which IFC’s funds cannot finance. It is available at [https://bit.ly/3qJDHSw](https://bit.ly/3qJDHSw)
47 ESRP (2016), 3.4.4.
48 IFC Sustainability Policy 2012, para 22.
E&S risk or hold detailed meetings with client management and staff in key departments to understand how it manages E&S risks in its investments.

IFC’s preliminary assessment found that PSBC lacked capacity to assess and manage the E&S risks of its lending activities. It also identified potential implementation challenges related to the significant size, structure, geographic reach and diversity of the client’s lending business.

IFC nevertheless went ahead with the 2015 equity investment, resulting in exposure to all of PSBC’s banking business. While the majority of PSBC borrowers are MSMEs and individuals, the client also lends to large businesses involved in activities with higher levels of E&S risk. On this basis, IFC categorized the E&S risk of the investment as FI-1 (high risk). In reviewing the client’s capacity to manage E&S risks, IFC stated that the client had “implemented procedures to comply with national laws including China’s Green Credit policy requirements, but it hasn’t developed a systematic approach including capacity for E&S management yet”. IFC undertook to provide technical support to PSBC in the development of its ESMS.49

For its part, the client agreed to the following IFC E&S Requirements:

- To implement an ESMS across all existing and future financing operations; and
- To ensure all existing and future financing operations comply with the IFC Exclusion List,50 applicable national law, and IFC Performance Standards.

The legal agreement between IFC and PSBC did not mention any exception to the application of IFC Performance Standards. Indeed, PSBC committed to apply IFC’s Performance Standards to all of its financing operations.

In addition, the agreement included an Environmental and Social Action Plan which required PSBC to take the following timely actions after IFC made its investment:

- Complete a diagnosis of its existing E&S practices within six months;
- Develop an ESMS and build staff capacity to implement the ESMS within 12-15 months;
- Start implementing the ESMS within 18 months; and
- Implement the ESMS client-wide for all new and existing loans within 24 months.51

Limitations on IFC’s access to information from PSBC were also reflected in the project’s reporting structures. In contrast to its usual practice, IFC took into account disclosure restrictions under Chinese law and agreed not to require PSBC to report to IFC any details of its individual loans or E&S incidents associated with its borrowers. IFC correctly noted at the time that this would limit its understanding of PSBC’s portfolio, including in relation to E&S risks.

Between June and September 2015, IFC secured approval of and committed to the PSBC investment.52

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49 IFC Summary of Investment Information (SII), Project 35461, Postal Saving Bank of China, at: https://bit.ly/3MenP2k
50 The Exclusion List defines the types of projects that IFC does not finance, available at https://bit.ly/3qJDHSw.
51 IFC Summary of Investment Information (SII), Project 35461, Postal Saving Bank of China.
52 IFC Summary of Investment Information (SII), Project 35461, Postal Saving Bank of China.
In conclusion, IFC appropriately categorized the E&S risk as FI-1 (high-risk) and required PSBC to implement an ESMS over 24 months. In a context where IFC had limited access to information about E&S risks in the potential client’s portfolio, IFC went beyond the requirements of the Sustainability Policy by requiring PSBC to apply the Performance Standards to all financing operations. IFC also set relevant E&S requirements for the investment following its Sustainability Policy. However, IFC also agreed to unusual limitations on access to client information regarding existing E&S risk in its portfolio and reporting, and deferred a more detailed diagnostic of the client’s E&S systems until after investment. As a result, it is not clear how IFC could reach the conclusion that PSBC would be in a position to meet IFC’s E&S requirements within a reasonable period – a key IFC Sustainability Policy (para. 22) threshold to move forward with an investment. This amounts to a preliminary indication of non-compliance in IFC’s pre-investment review of PSBC.

**IFC supervision**

IFC’s supervision of an investment begins at first disbursement and continues until the investment is closed. IFC supervises a financial intermediary’s implementation of its E&S requirements as set out in the investment agreement and Environmental and Social Action Plan (ESAP). IFC’s key supervision roles are to assess:

- The client’s level of compliance with the E&S requirements including all conditions of disbursement, ESAP items and other E&S covenants included in the legal agreement – including Performance Standards where applicable;
- Whether the FI is implementing an ESMS as envisaged at the time of IFC’s pre-investment review; and
- Whether there is sufficient evidence that the client has applied applicable E&S requirements to the business activities it finances.\(^{53}\)

IFC supervision activities include site visits to the financial intermediary client and where necessary the businesses it finances, particularly high-risk sub-projects.\(^{54}\) The frequency and focus of supervision should be commensurate with the identified E&S risk profile of the investment.\(^{55}\) IFC’s E&S Review Procedures also enable IFC to conduct reviews of FI loan files to ascertain whether the FI is implementing IFC’s E&S Requirements.\(^{56}\)

In December 2015, IFC completed its first disbursement to PSBC and acquired equity in the client. After completing a diagnostic of PSBC’s approach to E&S risk management in May 2016, which highlighted the client’s limited practice of E&S risk management and capacity to conduct E&S due diligence, IFC began supporting the bank’s ESMS development and efforts to strengthen risk management.

In 2018, PSBC launched its ESMS (Regulation on Environmental and Social Risk Management of Postal Savings Bank of China), committing to a comprehensive approach to E&S risk

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\(^{53}\) Sustainability Policy para 24 and 45. ESRPs 2014 and 2016, paras. 9.2.1 and 9.2.5.
\(^{54}\) IFC Sustainability Policy 2012, para. 45, and IFC E&S Review Procedures 2014, para. 9.2.5.
\(^{55}\) IFC Sustainability Policy, para. 45.
\(^{56}\) IFC Environmental and Social Review Procedures (2016), para. 9.2.9.
management. The ESMS includes issues covered in the IFC Performance Standards among those to be assessed in PSBC’s E&S due diligence of its portfolio. However, it does not specifically reference either IFC’s Performance Standards or its Exclusion List.

From 2016-2021, PSBC reported on its ESMS implementation in annual reports to IFC. In 2020, the client stated that it had over 100 Category A (high-risk) corporate investments and over 1,000 Category B (medium risk) investments. IFC supervision of the client’s E&S performance from 2016 to 2021 consistently reports that PSBC had established a comprehensive ESMS consistent with IFC’s requirements and commensurate with its business scope and activities.

However, based on a preliminary review of project files, CAO identified several factors that call into question IFC’s stated confidence in the client’s management of E&S risk in accordance with IFC requirements:

- PSBC’s E&S Management System does not refer to or require the application of the Performance Standards to its financing operations as required by its investment agreement with IFC.
- Available supervision documentation does not include evidence that the client is applying the Performance Standards to its investments. PSBC has a large portfolio of high and medium risk investments, all of which would require application of the Performance Standards under IFC’s Sustainability Policy. The samples of E&S due diligence on selected projects shared by PSBC with IFC include limited E&S analysis and do not offer sufficient evidence that PSBC applied the Performance Standards in its due diligence process for these investments.
- PSBC’s E&S Management System makes no reference to IFC’s Exclusion List and IFC does not appear to have commented on client financing of activities on the Exclusion List.

Taken together, these factors provide indications that IFC may not have complied with its obligation to supervise PSBC’s ESMS implementation in line with Sustainability Policy requirements and investment agreement terms.

c) Plausible Link between Alleged Harm and Potential Non-compliance

A compliance appraisal must consider whether the harm alleged in a complaint is plausibly linked to potential non-compliance. CAO concludes that there is a plausible link between the alleged harm raised by the complainants regarding the DPM mine and potential non-compliance in IFC’s review and supervision of its investment in PSBC.

The rationale for establishing a plausible link is as follows:

- IFC’s investment agreement required PSBC to apply the Performance Standards to all financing operations.
- PSBC provided financing to CNMC and NFC in the form of working capital loans. This should have triggered application of the Performance Standards, as discussed further below.

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• There are indications that IFC did not supervise PSBC’s application of the Performance Standards to its financing operations in general or ascertain whether PSBC was applying the Performance Standards to loans to NFC and CNMC in particular.
• NFC has effective control of DPM and is specifically responsible for the construction of the mine.
• The alleged harm to the complainants relates to issues covered by IFC’s Performance Standards.

In this case, five IFC Performance Standards are relevant, as follows:

• **PS1 (Assessment and Management of Environmental and Social Risks and Impacts)** in relation to the conduct of an appropriate environmental and social impact assessment and management of identified impacts and risks consistent with good international industry practice for the tailings dam; the disclosure of the EIA and revised addenda; and stakeholder engagement with potentially affected communities.
• **PS3 (Resource Efficiency and Pollution Prevention)** in relation to water and land contamination associated with the tailings dam’s operation and potential failure.
• **PS4 (Community Health, Safety, and Security)** in relation to community health and safety in the event of the tailings dam’s failure and location of the explosive storage facility.
• **PS6 (Biodiversity Conservation and Sustainable Management of Living Natural Resources)** in relation to biodiversity risks in the event of the tailings dam’s failure.
• **PS7 (Indigenous Peoples)** in relation to the complainants’ claims that they should be treated as Indigenous Peoples.

**CAO view on IFC and PSBC responses regarding lack of a plausible link**

In their responses, both IFC and PSBC rejected a plausible link between the alleged harm to the complainants and IFC non-compliance. They presented four main arguments in relation to this compliance criterion. These are summarized below alongside CAO’s evaluation of each argument.

*Claim there is no link between PSBC financing and DPM*

IFC and PSBC hold the view that there is no link between PSBC and DPM due to use of proceeds restrictions. In making this argument they cite Chinese law which states that working capital loans cannot be used for fixed assets, equity, or capital investment. IFC holds the view that national legal and regulatory requirements prohibit the use of working capital loan proceeds for investment in an enterprise outside China. PSBC also asserts that NFC and CNMC have confirmed that they did not in fact use its loans for the DPM project.

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58 During CAO’s complaint eligibility and assessment phase, IFC and PSBC noted to CAO the national law restrictions on working capital loans. CAO considered these points during its eligibility and assessment phases, and again during this compliance appraisal.

Working capital loans are corporate debt borrowings that companies use to finance operating expenses. While they cannot be used to buy long-term assets or make investments, they can cover a company’s short-term operational needs such as payroll, rent, and other operational costs and manage cash flow gaps during a business’s slow season. It is in the context of “day-to-day operations” that the link between PSBC financing and DPM is examined.

PSBC’s client, NFC, controls DPM and is the mine project’s engineering, procurement and construction (EPC) contractor. When it became majority owner of DPM in September 2018, NFC reported that it “dispatched directors and management personnel to the subsidiary to fully control the company’s operation and management.” NFC is therefore responsible for many aspects of the DPM project. These include plant engineering, procurement of supplies, and construction, installation and commissioning supervision of most aspects of the project, including the underground and surface facilities, tailings storage facility and transmission pipeline, process plant and related utilities, and plant water source and supply system.

NFC’s business activities to support DPM were within the potential use of proceeds of PSBC’s working capital loans to NFC. By providing working capital to NFC, PSBC became financially exposed to its investee’s general operations, including activities related to engineering, procurement and construction for the DPM project.

Chinese law referenced by IFC and PSBC prevents the use of working capital funds to finance fixed assets, equity, or capital investments. However, these same provisions of Chinese law do not include a restriction on the use of working capital funds to support business activities outside China.

Considering that NFC is the majority owner of DPM and has responsibility for operating and managing the development of the mine, NFC’s role in the mine’s development goes beyond the provision of fixed assets, equity, and capital. Accordingly, the restrictions on use of proceeds for working capital loans under Chinese law referenced by IFC and PSBC do not rule out the link between PSBC’s financing of NFC and development of the DPM mine.

Claim that IFC Performance Standards do not apply to Working Capital Loans

PSBC cites an IFC Financial Intermediary (FI) Interpretation Note to assert that the Performance Standards did not apply to working capital loans such as those it provided to NFC and CNMC. The Note states that an FI should apply the Performance Standards to project or long-term (over 36 months) corporate finance where the business activity includes higher E&S risks.

PSBC argues (section 3b, Client Response) that this provision does not apply to its short-term operational loans to CNMC and NFC.
However, this Interpretation Note is a guidance document on the application of IFC’s E&S Requirements and is not binding on IFC or its clients. The primary binding requirements in this case are the Sustainability Policy (binding on IFC) and the investment agreement (binding on IFC and the client). As noted above, IFC’s investment agreement requires PSBC to apply its E&S requirements, including the Performance Standards, to all financing operations. Neither the investment agreement nor the IFC Sustainability Framework provide a carve-out for working capital loans. The Sustainability Policy directs IFC to ensure an FI client applies the Performance Standards to higher risk business activities that they finance. Due to their involvement in mining, the business activities of CNMC and NFC should be considered to have higher levels of E&S risk. Based on the Sustainability Policy and the investment agreement, CAO concludes that the Performance Standards are likely to have been applicable to the corporate working capital loans PSBC provided to CNMC and NFC.

Claim that DPM does not qualify as a ‘sub-project’ or ‘sub-client’ under the CAO Policy

PSBC argues that it has no linkages to the DPM mine on the grounds that Dairi Prima Mineral is a fourth-tier subsidiary of CNMC and a third-tier subsidiary of NFC rather than a sub-project or sub-client. The CAO Policy states that CAO will assess, as relevant, IFC/MIGA’s review and supervision of its E&S Requirements at the Project or Sub-Project-level and consider Project or Sub-Project-level E&S performance. In this instance:

- IFC’s project is its investment in PSBC;
- CNMC and NFC are sub-clients of PSBC; and
- The sub-project is defined in CAO Policy as the business operations of a sub-client.

In deciding whether the business activity subject to a CAO complaint qualifies as a business operation of a sub-client, CAO assesses both the sub-client’s involvement in and/or leverage over the operations of the business activity and the importance of the business activity to the sub-client’s operations. In this context, CAO considers DPM to be a business activity of NFC given NFC’s majority ownership in the mining company, its role as the site’s EPC contractor, and its public statements regarding its active role in the project.

Claim that there is no direct linkage between PSBC and DPM according to international good practice standards

PSBC also cites provisions from the United Nations Guiding Principles on Business and Human Rights (UNGPs) and the OECD Guidelines for Multinational Enterprises (OECD Guidelines) to

65 CAO Policy, Section X, paras. 77.
66 CAO Policy defines project as: (1) With respect to investment services or advisory services provided by IFC to a Client, the investment or advisory services contemplated by the relevant services agreement; and (2) with respect to financing or investment engagements, the business activities that are contemplated or may be supported under the applicable Project agreements. Where relevant engagements or agreements have not been definitively agreed or executed, Project means the services, project or activities being discussed or contemplated by IFC and the Client.
67 CAO Policy defines sub-client as A business directly supported by an FI Client that is within the use of proceeds requirements in IFC’s finance or investment documents or MIGA’s contract of guarantee.
68 CAO Policy defines sub-project as A business operation of a Sub-Client within the use of proceeds requirements in IFC’s finance or investment documents or MIGA’s contract of guarantee. CAO Policy, Glossary.
argue that there is no “direct linkage” between PSBC and DPM and related E&S risks and impacts. 69

This issue is not directly relevant to the outcome of a compliance appraisal as the CAO Policy does not refer to the requirement of “direct linkage.” This said, a core principle guiding CAO's work is consistency with good practice, ... including the responsibility of business to respect human rights. 70 Thus, CAO is inclined to interpret its Policy in a manner that is consistent with established business and human rights standards. 71 These standards recognize that a business enterprise can be directly linked to adverse E&S risks and impacts through its business relationships, which include businesses numerous tiers down a value chain. 72 Moreover, when viewing direct linkage, these standards do not envisage any categorical carving out of operations or – in the case of financial institutions – of specific financial instruments, such as working capital loans. 73

Applying this approach, PSBC's working capital loans to NFC and CNMC establish business relationships which in turn provide the basis for a direct linkage between PSBC and harm potentially caused by the DPM mine.

d) Additional Appraisal Considerations: IFC Exit

When CAO prepared this compliance appraisal report in June 2022, IFC held an active investment in Postal Services Bank of China. However, PSBC reported during the appraisal process that it no longer has active loans to either CNMC or NFC. This circumstance triggers the provisions of the CAO Policy that apply to an IFC Exit. Specifically, the policy requires CAO to consider: For any Project or Sub-Project where an IFC/MIGA Exit has occurred at the time CAO completes its compliance appraisal, whether an investigation would provide particular value in terms of accountability, learning, or remedial action despite an IFC/MIGA Exit. (CAO Policy, para. 92)

An IFC Exit is defined as: With respect to any Project, the earlier of (i) the termination of the financing, investment, or advisory relationship with the Client for such Project pursuant to the applicable Project agreements; or (ii) when the Project ceases to exist, or the Project has been dropped by IFC after Board approval. (CAO Policy, definitions).

This provision gives CAO discretion to determine the value of conducting a compliance investigation where there is no longer an active financial relationship between IFC and the business activity that is subject to a complaint.

69 Client Response Regarding Concerns in Relation to IFC’s Investment (#35461), February 11, 2022, paras. 23 to 25 (see Appendix C). IFC response does not discuss the application of the UNGPs or the OECD Guidelines.
70 CAO Policy, para 10(g); see also para 5.
71 The main global standards on business and human rights are the OECD Guidelines for Multinational Enterprises and the United Nations Guiding Principles on Business and Human Rights (UNGPs), adopted in 2011. The OECD Guidelines were last updated in 2011 and include a chapter on human rights that is fully aligned with the UNGPs. The standards are available at: https://www.oecd.org/corporate/mne/ and https://www.ohchr.org/sites/default/files/documents/publications/guidingprinciplesbusinesshr_en.pdf
73 OHCHR response to request from BankTrack and OECD Watch for advice regarding the application of the UN Guiding Principles on Business and Human Rights where private sector banks act as nominee shareholders, August 30, 2021, p.4.
In this case, although the criteria for a compliance investigation are met, CAO has decided not to initiate a compliance investigation as there is no longer a financial connection between PSBC and the DPM mine. In reaching this decision, CAO followed the policy and considered whether there would be particular value of an investigation in terms of accountability, learning or remedial action despite the exit. Relevant factors included:

- The lack of an ongoing financing relationship between PSBC and CNMC or NFC which may make remedial action to address any CAO findings of harm or potential harm more difficult to achieve.
- The shortcomings indicated in IFC’s E&S review and supervision of PSBC, leading to a lack of application of the Performance Standards to sub-projects, are similar to those CAO has found in other IFC investments in large banks involved in corporate lending. As a result, CAO considers that this issue may be better dealt with as part of CAO’s ongoing compliance monitoring of IFC’s financial intermediary portfolio, rather than a specific investigation in response to this complaint.

6. CAO Decision

This section presents CAO’s decision on whether the matters raised in the complaint merit a compliance investigation based on the appraisal criteria and other considerations outlined in the CAO Policy.

Based on the analysis detailed in this appraisal report, CAO concludes that:

1. There are preliminary indications of potential harm to the complainants;
2. There are preliminary indications that IFC/MIGA may not have complied with its E&S Policies in exercising its responsibilities concerning its investment in PSBC; and
3. The alleged potential harm to the complainants is plausibly linked to IFC/MIGA’s potential non-compliance.

However, at the time of preparation of this compliance appraisal, IFC no longer has an active exposure to the DPM mine via its investment in PSBC. In this context, the CAO Policy requires consideration of whether an investigation would provide particular value in terms of accountability, learning, or remedial action despite an IFC Exit. For reasons outlined in section 5d, CAO has decided not to trigger a compliance investigation since there is no current financial exposure by PSBC to DPM.

CAO’s appraisal decision does not preclude future complaints related to the project or sub-project based on new circumstances, knowledge, or alleged harms/potential harms not known at the time of this report’s completion.

74 CAO’s FI Audit 2012 and subsequent monitoring reports (2014, 2015, 2017) have consistently noted that IFC does not, in general, have a basis to assess FI clients’ compliance with its E&S requirements. Available at https://bit.ly/3wLnRKu
75 CAO FI Audit case available at: https://bit.ly/3wLnRKu
In accordance with the CAO Policy, this appraisal report was shared with the Board, the World Bank Group President, IFC/MIGA Management, the client, and the complainants. The report is also publicly available, along with the IFC Management response and client response, on the CAO website.\textsuperscript{76}

\textsuperscript{76} CAO Policy, Sec. X, para. 106.
Appendix A: Complaint to CAO

Osvaldo Gratacós  
Vice President and CAO  
Office of the Compliance Advisor Ombudsman  
International Finance Corporation  
2121 Pennsylvania Avenue NW  
Washington, DC 20433 AS  

Email: CAO@worldbankgroup.org

29 October 2019

Dear Vice President Gratacós

Re: Complaint concerning IFC investments in:
- PT Dairi Prima Minerals (DPM),

1. We are the representatives of five villages in the regency of Diari, North Sumatra, Indonesia. Our villages are Bongkaras Village and Pandiangan Village. We are aware of other communities facing similar issues as below at the hands of the same corporation.

2. Due to concerns for our personal security, we request that our names be kept confidential.

3. We have limited reliable access to email or postal systems. Therefore, we request that you direct all correspondence related to the complaint to our advisors:
   - Natalie Bugalski, Legal Director, Inclusive Development International (Natalie@inclusivedevelopment.net)
   - David Pred, Executive Director, Inclusive Development International (David@inclusivedevelopment.net)

   The above individuals will ensure that information related to this complaint reaches us.

4. Inclusive Development International (IDI) is an international human rights organization that works to make the international economic system more just and inclusive. IDI supports and builds the capacity of grassroots organizations and affected communities to defend their rights and the environment against threats from transnational investment and destructive mega-projects.

5. We are likely to be, adversely affected by Dairi Prima Mineral’s Zinc/lead mine, and its associated facilities, which we believe to be an IFC sub-project.

6. We believe that the IFC is actively exposed to the DPM mine through its financial intermediary investments in Raiffeisen Bank and Postal Savings Bank of China, as set out and explained by a separate note by Inclusive Development International.
We believe we have not been properly consulted about the proposed DPM mine and will be adversely affected by numerous social and environmental impacts of the project:

- The mining company has not yet acquired a study on the risks from mining activities around disaster-prone and earthquake-prone areas.
- The company uses the Protected Forest Area for infrastructure development, and concern arises over the fact that this forest conversion will cause disturbance to our water resources.
- The mine will create a tailings dam that will cause chemical contamination. The whole mine is located in an area which has a significant earthquake risk.
- DPM are already bringing in external people from other provinces and countries to work the mine. This does and will place significant social pressure on our communities.
- The mine is likely to generate a large amount of air pollution which could lead to an increase in health problems for nearby communities.
- The mine will dramatically increase the heavy road traffic to and from the mine. This will be on public roads with communities located aside those roads.
- DPM have not conducted an EIA for the mine extraction phase and they have refused to provide adequate information about the mine. This is something we have tried to address through the Indonesian Information Commissioner, to date with no result.

We thank you in advance and look forward to hearing your response. If our complaint is found eligible, we would be pleased to add more information regarding previous, current and predicted impacts.

RAINIM PURBA
Pandiangan Village
Osvaldo Gratacós  
Wakil Presiden dan CAO  
Kantor Compliance Advisor Ombudsman International  
Finance Corporation  
2121 Pennsylvania Avenue NW  
Washington, DC 20433 AS  

Surel: CAO@worldbankgroup.org

29 Oktober 2019

Wakil Presiden Gratacós yang terhormat

Perihal: Pengaduan tentang investasi IFC di:  
- PT Dairi Prima Minerals (DPM),


2. Untuk menjaga keamanan pribadi kami, kami minta agar nama kami dirahasiakan.

3. Kami memiliki akses terbatas pada sistem surel dan pos yang bisa diandalkan. terkait dengan hal tersebut, segala bentuk korespondensi terkait dengan pengaduan, mohon ditujukan kepada penasihat kami:

   - Natalie Bugalski, Direktur Legal, Inclusive Development International  
     (Natalie@inclusivedevelopment.net)
   - David Pred, Direktur Eksekutif, Inclusive Development International  
     (David@inclusivedevelopment.net)

Para individu di atas akan memastikan bahwa informasi yang terkait dengan pengaduan ini tersampaikan kepada kami.

4. Inclusive Development International (IDI) merupakan senubuh organisasi hak asasi manusia internasional yang berupaya mewujudkan sistem ekonomi internasional yang lebih adil dan inklusif. IDI mendukung dan membangun kapasitas organisasi akar rumput dan masyarakat yang terdampak dalam rangka mempertahankan hak-hak dan lingkungan mereka terhadap ancaman kegiatan investasi transnasional dan mega proyek yang merusak.

5. Kami berpeluang besar terkena dampak merugikan tambang seng/timah PT Dairi Prima Mineral, dan fasilitas terkait miliknya, yang kami yakini adalah sub-proyek IFC.

Sepengetahuan kami, kami belum pernah diajak berdiskusi mengenai tambang DPM yang diusulkan dan kami akan terkena dampak merugikan dari berbagai dampak sosial dan lingkungan proyek:

- Perusahaan tambang tidak memiliki kajian tentang risiko dari kegiatan perusahaan tambang di kawasan rawan bencana dan rawan gempa.
- Perusahaan menggunakan kawasan Hutan Lindung untuk kepentingan pembangunan infrastruktur, dan dikuatirkan alih fungsi hutan lindung akan berpengaruh terganggunya sumber air kami.
- Tambang akan menciptakan tanggul tailing yang akan menyebabkan kontaminasi bahan kimia. Seluruh tambang terletak di daerah yang memiliki risiko besar gempa bumi.
- DPM sudah mendatangkan orang-orang luar dari provinsi dan negara lain untuk mengerjakan tambang. Hal ini akan memberikan tekanan sosial yang cukup besar pada masyarakat kami.
- Tambang berpeluang besar menghasilkan polusi udara dalam jumlah besar yang dapat menyebabkan peningkatan masalah kesehatan bagi masyarakat di sekitarnya.
- Tambang akan membuka arus lalu lintas jalan meningkat padat ke dan dari tambang. Lokasi ini di jalan umum dengan masyarakat tinggal di pinggir jalan tersebut.
- DPM belum melakukan AMDAL untuk tahap ekstraksi tambangnya dan mereka menolak memberikan informasi yang memadai tentang tambang. Masalah ini telah kami coba atasi melalui Komisi Informasi Pusat Indonesia, tetapi hingga saat ini tidak ada hasilnya.

Kami berterima kasih sebelumnya dan menantikan tanggapan Anda. Jika pengaduan kami dinilai memenuhi persyaratan, kami akan dengan senang hati menambahkan lebih banyak informasi mengenai dampak baik sebelumnya, saat ini, maupun prediksi nantinya.

[Signature]

RAINIM PURBA
Desa Pandiangan
Annex 1: Financial links between the IFC and PT Dairi Prima Mineral

The IFC is materially exposed to PT Dairi Prima Mineral through equity investments in two commercial banks: Raiffeisen Bank International of Austria and Postal Savings Bank of China. These banks have in turn made equity and debt investments in the Indonesian mining company Bumi Resources and the China Nonferrous mining group, respectively, which are the sole equity investors in PT Dairi Prima Mineral, the special project vehicle developing the mine in North Sumatra. The IFC’s exposure to the mine through these financial intermediary investments is detailed below.

1) Raiffeisen Bank International → Bumi Resources

In January 2014, the IFC made a $186.05 million equity investment in Raiffeisen Bank International. This investment exposes the IFC to Raiffeisen Bank International’s entire balance sheet, including the bank’s equity and debt investments in Bumi Resources, a beneficial owner of PT Dairi Prima Mineral.

While the IFC Project Information Portal claims that Raiffeisen Bank International “confirmed to IFC that it will deploy” the capital to four banking subsidiaries in Europe, the portal nonetheless makes clear that the IFC deal is a “straight equity investment” in Raiffeisen Bank International – not the four subsidiaries.

Indeed, the IFC’s investment was designed to directly benefit Raiffeisen Bank International. The investment contributed to the Austrian bank’s accelerated book building transaction in 2014, which was designed to help the bank repay $2.5 billion in assistance it received following the 2008 financial crisis and comply with Basel III requirements. The IFC’s investment in Raiffeisen Bank International gives it an ownership stake in the bank, commensurate shareholder voting rights and a proportion of the bank’s profits in the form of dividends. Equity investments of this nature cannot be ringfenced.

On June 12, 2014, six months after becoming an IFC financial intermediary client, Raiffeisen Bank International provided the Indonesian mining company Bumi Resources with an “AS$80 million [sic] loan. Five months later, Bumi Resources defaulted on the loan. Following a settlement agreement, 57.03% of the loan was converted into shares, giving Raiffeisen Bank International a significant equity stake in Bumi Resources. The remaining balance of the loan was converted into two new Bumi Resources debt facilities held by Raiffeisen Bank International: a credit facility with a maturity of 2021 and a convertible facility with a maturity of 2024 that could be redeemed for further equity in Bumi Resources.3

1 IFC Project Information Portal, Project #31979. https://disclosures.ifc.org/#/projectDetail/SII/31979
Bumi Resources is the self-described “parent company” of Bumi Resources Minerals, with a 35.73% equity stake in the subsidiary. Bumi Resources Minerals in turn owns a 49% equity stake in PT Dairi Prima Mineral. Through this relationship, Bumi Resources publicly acknowledges that it is a 17.51% beneficial owner of PT Dairi Prima Mineral. This chain of equity investments – from the IFC to Raiffeisen Bank International to Bumi Resources to Bumi Resources Minerals to PT Dairi Prima Mineral – creates sufficient materiality to expose the IFC to PT Dairi Prima Minerals. Moreover, Bumi Resources’ sole business activity is mining, a high-risk activity that necessitated a high level of social and environmental due diligence by Raiffeisen Bank International, which it apparently failed to apply.

While this chain of equity investments alone is enough to materially expose the IFC to PT Dairi Prima Mineral, a number of additional factors strengthen the exposure:

- Bumi Resources is one of the largest creditors of Bumi Resources Minerals, having provided its subsidiary with a working capital loan that has a current balance of $68 million. Moreover, as part of a cooperation agreement signed between the two entities, Bumi Resources administers the funds of Bumi Resources Minerals, suggesting it has a level of financial control over the company. This establishes active financial and administrative links between the two entities that go beyond the parent-subsidiary relationship.

- As part of that same cooperation agreement, Bumi Resources is providing “technical and project support” to Bumi Resources Minerals. PT Dairi Prima Mineral is one of just three projects operated by Bumi Resources Minerals – and it is the furthest along in terms of development. This suggests that Bumi Resources is operationally involved in PT Dairi Prima Mineral at some level.

- Although PT Dairi Prima Mineral has not yet begun commercial extraction, Bumi Resources Minerals has to date spent $256 million on the project: $65 million to fund exploration and the development of mining infrastructure and $191 million to purchase equity in PT Dairi Prima Mineral. This establishes active financial exposure between Bumi Resources Minerals and PT Dairi Prima Mineral.

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• Bumi Resources publicly states that it owns a 35.73% stake in Bumi Resources Minerals. However, there is evidence suggesting that it may own a larger stake than it claims. For instance, the Indonesian Stock Exchange, where Bumi Resources Minerals is listed, currently describes Bumi Resources as a majority shareholder, with an 87.09% stake.  

• There is further evidence suggesting that Bumi Resources may own a larger stake than it claims. Historically, Bumi Resources majority owned Bumi Resources Minerals. But when Bumi Resources Minerals ran into debt trouble several years ago, a number of outside investors became shareholders of the company as part of a restructuring. However, these new investors have apparent links with a number of other companies connected to Bumi and/or Indonesia’s Bakrie family, which historically has controlled the Bumi group of companies. This suggests that Bumi and/or the Bakrie family may control a much larger stake in Bumi Resources Minerals than they disclose:

  o **Wexler Capital Pte: 13.23% stake in Bumi Resources Minerals**
    Wexler Capital is an investment vehicle established in Singapore in 2013. The firm’s only known business activity is its investment in Bumi Resources Minerals. Its registered address is Suite #03-05 at the International Plaza in Singapore. A number of Bumi Resources entities are also registered at the same office suite, including:

    1) Bumi Capital Pte Ltd., a subsidiary of Bumi Resources
    2) Bumi Investment Pte., a subsidiary of Bumi Resources
    3) Lemington Investments Pte. Ltd., a subsidiary of Bumi Resources Minerals
    4) Bumi Energy Resources Singapore Pte. Ltd.

  o **1st Financial Company Limited: 22.86% stake in Bumi Resources Minerals**

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13 Singapore Databases, Bumi Capital PTE. Ltd. [https://www.singaporedatabases.com/company/200804179N/bumi-capital-pte-ltd](https://www.singaporedatabases.com/company/200804179N/bumi-capital-pte-ltd)


1. Financial Company Limited's registered address is the first floor of the Oliaji Trade Centre in Victoria, on Mahé Island, Seychelles. This is the same address of Zurich Assets International, a subsidiary of Bumi Resources.

- **PT Biofuel Indo Sumatra: 7.99% stake in Bumi Resources Minerals**
  The sole director of Biofuel Indo Sumatra is Bayu Irianto. He is also the president director of Bakrie Sumatera Plantations, a Bakrie Group subsidiary. Bayu Irianto’s official company biography notes that he has been with the Bakrie Group since 1997.

2) **Postal Savings Bank of China ➔ China Nonferrous**

In 2015, the IFC made a $300 million equity investment in Postal Savings Bank of China. This investment exposes the IFC to Postal Savings Bank's entire balance sheet. The bank’s balance sheet includes substantial debt investments in China Nonferrous Metal Mining (Group), the self-described parent company and largest shareholder of China Nonferrous Metal Industry’s Foreign Engineering and Construction Co., Ltd. (NFC), which in turn owns 51% of PT Dairi Prima Mineral.

In October and November of 2018, Postal Savings Bank co-arranged two perpetual medium-term note issues worth $721 million for China Nonferrous Metal Mining (Group) Co. In prospectuses accessed through the Bloomberg terminal, China Nonferrous Metal Mining (Group) Co. disclosed that it would use the capital from the issues to fund the operations of its subsidiaries. This would put NFC and PT Dairi Prima Mineral squarely within the stated use of proceeds for the debt issues.

Medium-term notes are debt instruments that create continuous active material exposure between the arranger, in this case Postal Savings Bank, and the issuer, in this case China Nonferrous Metal Mining (Group) Co. In a medium-term note transaction, the issuer does not sell all of the debt up front at once. Rather, the issuer continuously sells portions of the debt on an as-needed basis to the arranger, which then places the debt on the market, according to the issuer’s capital requirements. Through this relationship, the arranger regularly purchases debt from the issuer, creating ongoing intermittent exposure.

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26 IFC, Project Information Portal, #35461. <https://disclosures.ifc.org/#/projectDetail/SII/35461>


29 Bloomberg terminal
material exposure between the issuer and the arranger. The arranger is also expected to perform ongoing due diligence on the issuer over the life of the transaction.

The issuer may also call that debt, also on an as-needed basis, again depending on its capital requirements. In this way, arrangers of medium-term notes remain actively involved for the life of the transaction, acting as a conduit between the issuer and the market, with capital flowing back and forth continuously over time. The two medium-term notes issues by China Nonferrous Metal Mining (Group) Co. and managed by Postal Savings Bank in 2018 are unique in that they are perpetual, meaning that they never mature.

China Nonferrous Metal Mining (Group)’s sole business activity is mining and processing metals, high-risk activities that necessitated a high level of social and environmental due diligence by Postal Savings Bank, which the bank apparently failed to apply. Moreover, given the tenor (infinite) and size ($721 million) of the debt issue, Postal Savings Bank should have closely scrutinized the transaction for environmental and social risks.
This document is designed to supplement the complaint filed to the CAO on November 6, 2019, concerning the IFC’s material exposure to PT Dairi Prima Mineral through two financial intermediaries, Raiffeisen Bank International and Postal Savings Bank of China.

The IFC’s Material Exposure to PT Dairi Prima International through Raiffeisen Bank International:

In January 2014, the IFC made a $186.05 million “straight equity investment” in Raiffeisen Bank International.¹ On June 12, 2014, six months after becoming an IFC financial intermediary client, Raiffeisen Bank International provided the Indonesian mining company Bumi Resources with a loan worth “AS$80 million [note: presumably Australian dollars].”²

On November 14, 2014, Bumi Resources defaulted on the loan. Two years later, on November 9, 2016, Bumi Resources was forced to restructure to pay back Raiffeisen Bank International and its other creditors. The size of the Raiffeisen Bank International loan had reached AS$93.11 million. Under the terms of the restructuring agreement, Bumi Resources’ debt to Raiffeisen Bank International was converted into the following equity and debt instruments:³

- 57.03% of the total debt amount, roughly AS$53 million, was converted into shares in Bumi Resources. The size of Raiffeisen Bank International’s stake in Bumi Resources is not disclosed.⁴ However, given that the share price of Bumi Resources was 290 Indonesian Rupiah on November 9, 2016,⁵ the day the conversion occurred, Raiffeisen Bank International would have acquired approximately 1.84 billion shares in the company, based on currency exchange rates that day.⁶

- 32.24% of the debt was converted into a “New Senior Secured Facility and/or New 2021 Notes.”⁷ Based on the instrument’s name, this debt appears to have a maturity date of 2021.

- 10.73% of the debt was converted into seven-year mandatory convertible bonds, which mature in 2023.⁸ Because the conversion to shares is mandatory, Raiffeisen Bank International

¹ IFC Project Information Portal, Project #31979. https://disclosures.ifc.org/#/projectDetail/SII/31979
⁵ Thomson Eikon
⁶ XE, Australian dollar exchange rates on November 9, 2016, https://www.xe.com/currencytables/?from=AUD&date=2016-11-09
effectively took on an additional equity stake in Bumi Resources. However, the company has not disclosed whether the conversion occurred – and if it did, at what conversion rate.

Despite this restructuring, Bumi Resources’ debt troubles worsened. In May-June 2017, the company issued a limited public offering to its existing shareholders in an attempt to pay back debt amounting to US$4.2 billion.9 Under the terms of the offering, existing equity holders were entitled to roughly double their current shareholding.10 Based on the above calculations, Raiffeisen Bank International would have had a minimum of roughly 1.84 billion shares before the limited public offering (and more if it had converted the bonds it held). If it had participated in the rights issue, its equity holdings would have doubled to at least approximately 3.68 billion shares.

Bumi Resources currently has 65.48 billion shares outstanding.11 If Raiffeisen Bank International had participated in the 2017 rights issue, it would have a minimum stake in Bumi Resources of approximately 5.6%. If it didn’t participate, it would own a minimum of roughly 2.8% of the company.

Bumi Resources is the self-described “parent company” of Bumi Resources Minerals,12 with a 35.73% equity stake in its subsidiary. Bumi Resources Minerals in turn owns a 49% equity stake in PT Dairi Prima Mineral. Through this relationship, Bumi Resources describes itself as a 17.51% beneficial owner of PT Dairi Prima Mineral.13 This chain of equity investments, from the IFC through Raiffeisen Bank International and Bumi Resources, is alone enough to materially expose the IFC to PT Dairi Prima Mineral.

The following factors, which supplement those discussed in the annex to the complaint submitted to the CAO on November 6, 2019, strengthen this exposure:

- **Equity investments cannot be ringfenced:** When the IFC purchased common stock in Raiffeisen Bank International, it became part owner of the bank. The IFC is thus exposed to the Austrian bank’s entire balance sheet. This includes Raiffeisen Bank International’s loan to – and subsequent equity and debt investments in – Bumi Resources. As a shareholder of Raiffeisen Bank International, the IFC is part owner of the bank; receives a proportion of the bank’s profits in the form of dividends; has voting rights; and is entitled to a proportion of the bank’s net worth if its liabilities are settled and its assets are sold.14 Equity investments of this nature cannot be ringfenced.

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12 Bumi Resources Minerals, Annual Report 2018. [https://www.idx.co.id/StaticData/NewsAndAnnouncement/ANNOUNCEMENTSTOCK/From_EREP/201904/50cfb3d9b8_7a9fd8598b.pdf](https://www.idx.co.id/StaticData/NewsAndAnnouncement/ANNOUNCEMENTSTOCK/From_EREP/201904/50cfb3d9b8_7a9fd8598b.pdf)
The IFC is a shareholder in Raiffeisen Bank International, not its Eastern European subsidiaries: The IFC Project Information Portal claims that Raiffeisen Bank International “confirmed to IFC that it will deploy” the capital from this investment to four banking subsidiaries in Eastern Europe. However, the portal nonetheless makes clear that the IFC deal is a “straight equity investment” in Raiffeisen Bank International—not those four subsidiaries.\(^\text{15}\) If the IFC had wanted to invest directly in those subsidiaries, it could have done so. Indeed, the IFC has done just that on many occasions: It made nine direct investments in Raiffeisen Bank International’s Eastern European subsidiaries between 2000 and 2019.\(^\text{16}\) However, in this case, the IFC chose to purchase shares in Raiffeisen Bank International.

The IFC investment was designed to benefit Raiffeisen Bank International: The IFC invested directly in Raiffeisen Bank International—and not its subsidiaries—because the Austrian bank needed to be bailed out of financial troubles. The investment contributed to Raiffeisen Bank International’s accelerated book-building transaction in 2014, which was designed to help the Austrian bank repay $2.5 billion in assistance it received following the 2008 financial crisis. The IFC investment also helped the Austrian bank comply with Basel III requirements.\(^\text{17}\)

The IFC board had strong doubts about the investment: On June 21, 2012, the IFC Board of Directors voted on whether to approve the investment in Raiffeisen Bank International. Notably, the executive directors of Japan and the United States, Nobumitsu Hayashi and Ian Solomon, went on record opposing the investment, according to meeting minutes.\(^\text{18}\) Such public opposition to a proposed IFC investment by two prominent board members is unusual. That IFC funds were being used to bail out a large European commercial bank with extensive exposure to the tobacco industry, which is on the IFC’s exclusion list, and the Russian oil industry may have been of concern to Hayashi and Solomon.

Raiffeisen Bank International is not an unwitting equity investor in Bumi Resources: When Bumi Resources restructured for the first time, in November 2016, the company’s creditors voted on whether to approve the terms. One hundred percent of the company’s “concurrent creditors,” including Raiffeisen Bank International, approved the terms, including the conversion of some debt to equity. The second restructuring, in May-June 2017, involved a rights issue to existing shareholders. Raiffeisen Bank International had the option to decline additional shares; it is unclear what the bank ultimately decided. But in both cases, Raiffeisen Bank had full control over whether it acquired shares in Bumi Resources.\(^\text{19}\)

\(^{15}\) IFC Project Information Portal, Project #31979. [https://disclosures.ifc.org/#/projectDetail/SII/31979](https://disclosures.ifc.org/#/projectDetail/SII/31979)

\(^{16}\) IFC Project Information Portal. [https://disclosures.ifc.org](https://disclosures.ifc.org)


• **Bumi Resources is a mining company with a long track record of social and environmental problems:** Raiffeisen Bank International chose to finance Bumi Resources three times: When it provided the original loan in 2014, when it approved the conversion of that loan to equity and debt in 2016, and when it subscribed to the rights issue in 2017 (assuming it did). Bumi Resources has a well-documented track record of harmful social and environmental impacts, particularly on the island of Borneo, where it operates one of the world’s largest open-pit coal mines. The company’s past performance, along with the fact that its only business activities are in the high-risk mining industry, necessitated heightened due diligence by Raiffeisen Bank International. On all three occasions, the bank apparently failed to apply the necessary level of due diligence.

• **The IFC’s material exposure to PT Dairi Prima Mineral is neither diminutive nor remote, in the context of previous CAO eligibility determinations:** The IFC’s exposure to sub-projects can be measured in two ways: the proportional size of the IFC’s exposure and the IFC’s proximity to the sub-project on the ground. In the case of PT Dairi Prima Mineral, the size of Raiffeisen Bank International’s exposure to the project is at minimum between 0.49% and 0.98%, depending on whether the bank participated in the 2017 Bumi Resources rights issue. (Because the IFC does not disclose details on its equity investments in commercial banks, including the size of its equity stakes, it is not possible to measure the exposure back to the IFC.) In terms of proximity, there are three entities between the IFC and PT Dairi Prima Mineral: Raiffeisen Bank International, Bumi Resources and Bumi Resources Minerals.

![Diagram of exposure and layers]

The CAO has found at least one complaint eligible in which the size and proximity of the IFC’s exposure are comparable to that of PT Dairi Prima Mineral: Lower Sesan 2. (A lack of publicly disclosed information made it difficult to assess many of the financial-intermediary cases found eligible by the CAO.) The CAO found IFC material exposure in the Lower Sesan 2 case through two financial intermediaries:

- **Vietinbank:** The IFC’s client is Vietinbank. In 2014, Vietinbank signed an agreement...

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to provide debt to Electricity Vietnam worth $2.85 billion, or 13.6% of the company’s total debt liabilities of $20.97 billion (486.9 trillion VND) at the end of 2017, the latest date this information is available. At the time that the complaint was filed, Electricity Vietnam owned 43% of EVN International, which in turn owned a 10% stake in Lower Sesan 2. Through this relationship, the relative size of Vietinbank’s exposure to Lower Sesan 2 was 0.58%. This is comparable to the size of Raiffeisen Bank International’s exposure to PT Dairi Prima Mineral of between 0.49% and 0.98%. Moreover, there are three entities between the IFC and Lower Sesan 2, the same number that are between the IFC and PT Dairi Prima Mineral. Furthermore, while EVN International’s stake in Lower Sesan 2 is passive, Bumi Resources is operationally involved in PT Dairi Prima Mineral, arguably closing the distance between the two.

**ABBank:** The IFC’s client is ABBank. The Vietnamese bank owns a 10.31% stake in EVN International, which in turn owns a 10% stake in Lower Sesan 2. Through this relationship, the relative size of ABBank’s exposure to the dam is 1.03%. This is comparable to Raiffeisen Bank International’s exposure to PT Dairi Prima Mineral. Moreover, while EVN International’s stake in Lower Sesan 2 is passive, Bumi Resources is operationally involved in PT Dairi Prima Mineral, arguably closing the distance between the two.

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24 Thomson Eikon.

Table 1: Comparison of IFC’s Exposure to PT Dairi Prima Mineral and Lower Sesan 2

<table>
<thead>
<tr>
<th>Project</th>
<th>Financial Intermediary</th>
<th>Size of Financial Intermediary’s Exposure</th>
<th>Layers between IFC and Project</th>
<th>Sub-Client Involved in Project Operations?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dairi Prima Mineral</td>
<td>RBI</td>
<td>0.49% - 0.98%</td>
<td>3</td>
<td>Yes</td>
</tr>
<tr>
<td>Lower Sesan 2</td>
<td>Vietinbank</td>
<td>0.58%</td>
<td>3</td>
<td>No</td>
</tr>
<tr>
<td>Lower Sesan 2</td>
<td>ABBank</td>
<td>1.03%</td>
<td>2</td>
<td>No</td>
</tr>
</tbody>
</table>

- **The IFC’s exposure to PT Dairi Prima Mineral may be even greater, if Bumi Resources controls more of Bumi Resources Minerals than it discloses:** Bumi Resources publicly claims to own 35.73% of Bumi Resources Minerals shares. (Until a restructuring several years ago, it owned a majority stake.) But evidence exists that Bumi Resources may own a greater stake than it discloses. In Bumi Resources Minerals’ 2018 Annual Report, Bumi Resources is described as its “parent company.”

[T]he parent company *(induk perusahaan)* owns more than fifty percent of [the subsidiary’s] shares; (b) the parent company controls more than fifty percent of the voting rights in a general meeting of shareholders; and/or (c) the parent company influences management control, the appointment, and the dismissal of directors and commissioners.

This suggests that Bumi Resources owns and/or controls more than 50% of Bumi Resources Minerals’ shares and/or has sufficient influence over the management and directors of the company to regard itself as the parent, which would in turn increase the IFC’s exposure to PT...
Dairi Prima Minerals. It is possible that Bumi Resources is exercising this ownership/control surreptitiously.

- **Bumi Resources may majority-own or -control Bumi Resources Minerals through shell companies registered in tax havens:** When Bumi Resources sold its majority stake in Bumi Resources Minerals several years ago, a number of little-known companies registered in tax havens became large shareholders. These shell companies, which have no discernible business activity other than holding large stakes of Bumi Resources Minerals, share office suites with a number of entities connected to Bumi Resources and/or the Bakrie family (which controls Bumi Resources). This suggests that Bumi Resources may retain majority control over the company but is seeking to conceal this from the public.

For instance, Wexler Capital Pte., which owns 13.23% of Bumi Resources Minerals, shares the same office suite in Singapore with at least four Bumi Resources/Bakrie-connected entities: 1) Bumi Capital Pte Ltd., a subsidiary of Bumi Resources; 2) Bumi Investment Pte., a subsidiary of Bumi Resources; 3) Lemington Investments Pte. Ltd., a subsidiary of Bumi Resources Minerals; and Bumi Energy Resources Singapore Pte. Ltd. Other shareholders of Bumi Resources Minerals have similar connections to Bumi Resources/the Bakries.

This would not be the first time that the Bakrie family has sought to obscure its ownership stake in a company. In a dispute with a British investor for control over Bumi Resources several years ago, the Bakrie family used an unknown investment vehicle called Long Haul Holdings to wage that fight – without publicly disclosing its connection to the entity.

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**The IFC’s Material Exposure to PT Dairi Prima International through Postal Savings Bank of China:**

In 2015, the IFC made a $300 million equity investment in Postal Savings Bank of China. This investment exposes the IFC to Postal Savings Bank’s entire balance sheet. The bank’s balance sheet

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29 Singapore Databases, Bumi Capital PTE. Ltd. https://www.singaporedatabases.com/company/200804179N/bumi-capital-pte-ltd
37 IFC, Project Information Portal, #35461. https://disclosures.ifc.org/#!/projectDetail/SII/35461
includes substantial investments in China Nonferrous Metal Mining (Group) Co., the self-described parent company and largest shareholder of China Nonferrous Metal Industry’s Foreign Engineering and Construction Co., Ltd. (NFC), which in turn owns 51% of PT Dairi Prima Mineral.

In October and November of 2018, Postal Savings Bank co-arranged two perpetual medium-term note issues worth a total of $721 million for China Nonferrous Metal Mining. In prospectuses accessed through the Bloomberg terminal, China Nonferrous Metal Mining disclosed that it would use the capital from the issues to fund the operations of its subsidiaries. This would put NFC and PT Dairi Prima Mineral squarely within the stated use of proceeds for the securities issues.

This is the first complaint that the CAO has received involving perpetual medium-term notes. While the CAO has determined that bond underwriting does not materially expose the IFC in most cases, perpetual medium-term notes are structurally and categorically different from bonds. In addition, the OECD issued new guidance in October 2019 on the human rights and environmental responsibilities of securities underwriters; this guidance has particular relevance for arrangers of medium-term notes. For these reasons, the CAO should not apply its decision on bonds to perpetual medium-term notes. Rather, it should issue a new reasoned decision for this distinct instrument, given the following factors:

- **Arrangers of perpetual medium-term notes are involved in the issue continually and infinitely, creating ongoing material exposure until the end of the issue:** When underwriters issue bonds, they sell their entire allotment of securities up front, in one lump sum, after which their involvement ends. Arrangers of medium-term notes, on the other hand, continuously sell portions of the total amount over the life of the issue, depending on the issuer’s capital needs – and the market’s appetite for the securities. As the St. Louis Federal Reserve notes, medium-term notes give “a corporation the flexibility to issue in small amounts continuously.” It can be helpful to think of medium-term notes as the revolving credit facility of the fixed-income world. Indeed, the OECD, in its Glossary of Statistical Terms, refers to notes issued under a medium-term facility as “a form of revolving credit.”

China Nonferrous Metal Mining’s two perpetual medium-term notes issues are structured in this way. According to the prospectuses, the arrangers are responsible for selling the securities

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39 Bumi Resources Minerals, Annual Report 2018. [https://www.idx.co.id/StaticData/NewsAndAnnouncement/ANNOUNCEMENTSTOCK/From_EREP/201904/50cfb3df9b8_7a96f859fb.pdf](https://www.idx.co.id/StaticData/NewsAndAnnouncement/ANNOUNCEMENTSTOCK/From_EREP/201904/50cfb3df9b8_7a96f859fb.pdf)
40 Thomson Eikon.
41 Prospectuses accessed through the Bloomberg terminal: [中国有色矿业集团有限公司2018年度第三期中期票据募集说明书](https://www.idx.co.id/StaticData/NewsAndAnnouncement/ANNOUNCEMENTSTOCK/From_EREP/201904/50cfb3df9b8_7a96f859fb.pdf) pp. 15-16, 19, November 2018.
[中国有色矿业集团有限公司2018年度第二期中期票据募集说明书](https://www.idx.co.id/StaticData/NewsAndAnnouncement/ANNOUNCEMENTSTOCK/From_EREP/201904/50cfb3df9b8_7a96f859fb.pdf) pp. 18-19, October 2018.
on the market. As a co-arranger, Postal Savings Bank of China is thus responsible for selling an allotment of the securities to investors.

It is worth pointing out that like all securities issues, the China Nonferrous Metal Mining transactions utilize a bank to act as trustee. Shanghai Clearing House is the trustee of both transactions. As trustee, Shanghai Clearing House is not involved in selling the securities to investors. Rather, the trustee acts as an intermediary between the issuer and note holders, including monitoring compliance with the covenants and facilitating interest payments.

The issue period (the period during which the arrangers place the securities on the market) for both sets of notes is “3+N.” In this case, the “N” denotes the number of years before the securities mature. Since these securities are perpetual and never mature, the “N” denotes eternity. (The “3” in the equation means that China Nonferrous Metal Mining has the option to call the securities on the third year and for every year thereafter. If it does not, the coupon rate is recalculated and the issue continues in perpetuity.) In other words, Postal Savings Bank of China will be selling portions of the $721 million – the total amount of both issues – through 2021, and if the issue isn’t called, for eternity.

The structure of these perpetual medium-term notes thus creates active material exposure between Postal Savings Bank (and its shareholder the IFC) and China Nonferrous Metal Mining and its subsidiaries, including NFC and its Dairi Prima Mineral project.

- Under accounting standards, bonds and perpetual medium-term notes are categorized differently: Bonds are a form of debt. Perpetual notes, on the other hand, are categorized as equity-like instruments because they have the characteristics of shares. As noted by Reuters, “Under International Financial Reporting Standards, perpetual bonds count as equity as long as they do not have a set maturity and the call is an option of the issuer.” The European Financial Reporting Advisory Group, meanwhile, notes that instruments with no maturity date and in which interest payments are made at the discretion of the issuer have the characteristics of equity. The two 2018 China Nonferrous Metal Mining medium-term note have these three

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45 Prospectuses accessed through the Bloomberg terminal:
46 Bloomberg terminal.
48 China Nonferrous Mining Corporation, Annual Report 2017. Limited
http://www.cnemel.net/Managed/Resources/docs/report/ar2017e.pdf
https://www.efrags.org/article/idUSI-3N04CW11H520130409
50 Reuters, “Perpetual bonds arrive in China,” April 9, 2013.
https://www.reuters.com/article/idUSL3N0CW11H520130409
characteristics, according to the prospectuses: They have no set maturity date, the issuer has the option of calling them on the third year and for every year thereafter, and the issuer has the right to defer interest payments.\textsuperscript{52} Indeed, Chinese regulators have also historically viewed perpetual securities as equity-like. (New regulations may change this in some cases, although it is not clear yet what the new rules will mean in practice.\textsuperscript{53})

Because perpetual medium-term notes are \textit{categorically different} from bonds, the CAO should issue a new, distinct reasoned decision on whether they create material exposure for the IFC. The CAO should not apply its reasoned decision on bonds – which are debt – to an instrument that is classified as equity-like.

- \textbf{New OECD guidance clarifies the responsibility of underwriters for harmful human rights and environmental impacts:} In guidance issued in October 2019, the OECD makes clear that securities underwriters have a responsibility to address adverse impacts to which they are “directly linked.” By underwriting two China Nonferrous Metal Mining medium-term notes, whose proceeds are to be directed to the operations of its subsidiaries, Postal Savings Bank of China is directly linked with the potential impacts of the PT Dairi Prima Mineral project. The OECD guidance notes that a bank that is directly linked “has a responsibility to seek to prevent or mitigate the impact, using its leverage, which may involve efforts to influence the client to provide remediation.” The guidance acknowledges that leverage may be limited for underwriters of debt and equity transactions, because these issuances “do not provide long-term opportunities to maintain some degree of leverage over a client.”\textsuperscript{54} However, the situation for arrangers of medium-term notes is fundamentally different: Unlike bond underwriters, they maintain leverage over the issuer for the life of the transaction because they continuously sell portions of the medium term notes. Therefore, Postal Savings Bank of China has a responsibility – and the necessary leverage – to engage with China Nonferrous Metal Mining over the social and environmental risks of the PT Dairi Prima Mineral project.

\textsuperscript{52} China Nonferrous Mining Corporation, Annual Report 2017. Limited. \texttt{http://www.cnmcl.net/Managed/Resources/docs/report/ar2017e.pdf}
\textsuperscript{54} OECD, Due Diligence for Responsible Corporate Lending and Securities Underwriting, October 29, 2019. \texttt{https://www.oecd.org/investment/due-diligence-for-responsible-corporate-lending-and-securities-underwriting.htm}
Appendix B: Management Response

INTERNATIONAL FINANCE CORPORATION

MANAGEMENT RESPONSE
TO THE CAO COMPLAINT
ON

PSBC EQUITY
(PROJECT #35461)

February 11, 2022
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ABBREVIATIONS AND ACRONYMS

BR    Bumi Resources
BRM   Bumi Resources Minerals
CAO   Office of the Compliance Advisor Ombudsman
CBIRC China Banking and Insurance Regulatory Commission
CNMC  China Nonferrous Metal Mining (Group) Co., Ltd
DPM   PT Dairi Prima Mineral
E&S   Environmental and Social
ESMS  Environmental and Social Management System
IDI   Inclusive Development International
IFC   International Finance Corporation
MSME  Micro-, Small-, and Medium-sized Enterprise
MTN   Medium-term Note
NFC   China Nonferrous Metal Industry’s Foreign Engineering and Construction Co., Ltd
PRC   People’s Republic of China
PSBC  Postal Savings Bank of China
RBI   Raiffeisen Bank International
US$   United States Dollar
EXECUTIVE SUMMARY

i. This Management Response pertains to an October 2019 complaint submitted to CAO concerning alleged exposure of IFC, through IFC’s equity investments in Raiffeisen Bank International (RBI) and Postal Savings Bank of China (PSBC), to PT Dairi Prima Mineral (DPM) lead-zinc mine in Indonesia’s North Sumatra Province (the “Complaint”).

ii. The Complaint was filed by local communities near DPM, with support from a US-based civil society organization, Inclusive Development International (IDI), and several Indonesian civil society organizations. The Complaint claims that these local communities would be adversely affected by numerous environmental and social (E&S) impacts due to the proposed DPM mine, and that IFC is actively exposed to the mine through RBI and PSBC as following alleged links:

- RBI has both equity and debt investments in Bumi Resources (BR), an Indonesian mining company, which owns a 35.73% equity stake in Bumi Resources Minerals (BRM). BRM in turn owns a 49% equity stake in DPM.

- PSBC had substantial debt investments in China Nonferrous Metal Mining Group Co., Ltd (CNMC) through its participation in the arrangement of two perpetual medium-term note (MTN) issues for CNMC in October and November 2018. CNMC is the largest shareholder at a 33.75% equity stake of China Nonferrous Metal Industry’s Foreign Engineering and Construction Co., Ltd (NFC), which in turn owns a 51% equity stake in DPM.

iii. CAO found the Complaint eligible for assessment in March 2020 in relation to IFC’s investment in PSBC because “PSBC may have a debt exposure to CNMC and NFC.” CAO found the exposure of RBI not material to the Complaint.

iv. IFC made an equity investment equivalent to US$286 million in PSBC in December 2015, representing a 0.69% shareholding at that time. PSBC is a leading bank in China for Micro-, Small- and Medium-sized Enterprises (MSME) and rural finance. As of the date of this Management Response, IFC holds approximately 0.26% of the total shares of PSBC, which has a total market capitalization of approximately US$85 billion.

v. IFC takes seriously allegations in the Complaint related to E&S risks and impacts in the DPM mine, and is concerned especially by the fear of reprisals expressed by those making the complaint (the “Complainants”). IFC does not tolerate any action by an IFC client that amounts to retaliation – including threats, intimidation, harassment, or violence – against those who voice their opinion regarding the activities of IFC or our clients. Based on publicly available information, at the time of receiving the Complaint, the DPM mine was in a pre-construction phase. IFC has supported and fully cooperated with CAO in its assessment of the Complaint, including the facilitation of communications between PSBC and CAO.

vi. IFC has investigated the alleged financial link between PSBC and DPM to determine whether PSBC has direct or indirect financial exposure to DPM, the subject of the complaint, and
whether PSBC should have applied IFC E&S requirements to assess and mitigate the E&S risks and impacts associated with DPM. For (a) the alleged PSBC participation in the two MTNs issued by CNMC, the largest shareholder of NFC which in turn is the largest equity holder of DPM, and (b) CAO’s additional query of other possible financing provided by PSBC to CNMC and NFC, evidence shows that:

- (a) PSBC did not underwrite or invest in either of these two MTNs issued by CNMC. Though PSBC’s name was on the underwriting syndicate list, any qualified institution who is included in such list will be entitled, but not obliged, to subscribe to the MTNs in the book building process. This is corroborated by the disclosed subscription instructions of the two MTNs stating that each underwriting syndicate member’s minimum subscription amount is zero.

- (b) PSBC had provided only working capital loans to CNMC and NFC in the past. Under the laws of the People’s Republic of China (PRC) and regulatory framework applicable to the type of financing, such working capital loans were all short term in nature and must be used only for operating expenses and working capital purposes, and cannot be used for fixed assets, equity, or capital investment, e.g., overseas investment in DPM. PSBC currently has no outstanding loans with either CNMC or NFC. NFC, as an equity investor in DPM, also confirmed PSBC’s position that none of PSBC loans to NFC have been used for purposes relating to the DPM mine.

vii. Management therefore holds the view that there is no link between PSBC and DPM. All above supporting evidence clearly demonstrates that neither the two MTNs nor PSBC’s past short-term working capital loans to CNMC and NFC substantiate the alleged financial connection between IFC and DPM. Management therefore asserts that PSBC cannot be expected to require DPM to apply IFC E&S requirements, and that any alleged E&S risks and potential impacts related to DPM cannot be plausibly linked to either PSBC or IFC. Management believes that this Complaint does not satisfy CAO’s appraisal criteria for investigation which requires that such link be established as set forth in the 2021 CAO policy.

viii. Notwithstanding the above, Management respects CAO’s process in its assessment of the Complaint in relation to IFC’s investment in PSBC and will continue to cooperate with CAO during its compliance appraisal.

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1 IFC/MIGA Independent Accountability Mechanism (CAO) Policy, 2021, paragraph 91.
I. INTRODUCTION

1. In October 2019, the Complaint was lodged with CAO concerning Raiffeisen Bank International (RBI) and Postal Savings Bank of China (PSBC) financed by IFC.

2. In March 2020, CAO determined the Complaint eligible due to IFC’s investment in PSBC, while considering the exposure of RBI not material to the Complaint.

3. IFC takes seriously the allegations in the Complaint related to environmental and social (E&S) risks and impacts and is concerned especially by the fear of reprisals expressed by those making the complaint. IFC’s Position Statement on Retaliation Against Civil Society and Project Stakeholders makes clear that IFC does not tolerate any action by an IFC client that amounts to retaliation – including threats, intimidation, harassment, or violence – against those who voice their opinion regarding the activities of IFC or its clients. IFC has supported and fully cooperated with CAO in its assessment of the Complaint, including the facilitation of communications between PSBC and CAO.

4. Upon the request of CAO and IFC, PSBC provided relevant information and indicated that it does not have any financial exposure or link to the activities that allegedly caused the E&S risks and impacts cited in the Complaint. PSBC believes that the absence of such a connection means that the Complaint falls outside CAO’s mandate to further assess or handle the case.

5. Management has reviewed CAO’s Assessment Report for the Complaint regarding IFC’s investment in PSBC and prepared the following response. The subsequent sections provide brief descriptions of the Project background, the Complaint, IFC Management’s Response and the conclusion.

II. PROJECT BACKGROUND

6. **IFC Investment in PSBC.** In 2015, IFC’s Board of Directors approved an investment in PSBC, one of China’s largest banks and the leading local bank for Micro-, Small-, and Medium-sized Enterprises (MSME) and rural finance (the “Project”). The Project entailed an equity investment by IFC through the subscription of 474,290,000 common shares of PSBC for a cash consideration equivalent to US$286 million, which represented a 0.69% shareholding at that time.

7. PSBC was listed on the Hong Kong Exchange and Shanghai Stock Exchange in 2016 and 2020, respectively. As of the date of this Management Response, IFC holds approximately 0.26% of the total shares of PSBC, which has a total market capitalization of approximately US$85 billion.

8. **Project Context.** The Project aligns with the IFC Country Partnership Strategy for China (FY2013-2016) to contribute to the World Bank Group’s Universal Financial Access goal and China’s own efforts in expanding financial access and inclusion. It does so by focusing on balanced and inclusive rural-urban development to reduce the gap between living standards in urban and frontier areas, through investments and advisory work in MSME finance and rural finance.
9. **Project Purpose.** The Project provides a unique opportunity for IFC to support financial inclusion and poverty alleviation in China, given PSBC’s alignment with this mandate, its extensive outreach in the frontier regions to underserved MSMEs, and its potential growth with the introduction of new products and channels.

10. **Advisory Services.** In addition to the equity investment, IFC also provided a comprehensive advisory services package to PSBC in four areas: (i) Agriculture, Rural, and Farmer Finance; (ii) MSME Finance; (iii) Corporate Governance; and (iv) Environmental & Social Risk Management and Sustainable Finance. IFC’s advisory work with PSBC was completed by June 30, 2021. With IFC support and among others, PSBC has developed an environmental and social management system (ESMS) to screen and monitor its lending activities consistent with national laws and regulations and IFC requirements. PSBC has won many recognitions for its achievements in green financing, including the recent Global Green Finance Award by International Finance Forum in 2021.

### III. CAO COMPLAINT

11. On October 29, 2019, a complaint was lodged with CAO by representatives from two villages, Bongkaras Village and Pandiangan Village, on behalf of five villages in the regency of Diari, North Sumatra, Indonesia. The Complainants were assisted by a US-based civil society organization, Inclusive Development International (IDI), and several Indonesian civil society organizations, including BAKUMSU, a legal aid organization based in North Sumatra. The Complainants alleged that they had not been properly consulted about the proposed PT Dairi Prima Mineral (DPM) zinc and lead mine in Indonesia and would be adversely affected by numerous E&S risks and impacts stemming from the mine construction and operation. These included: (i) lack of a study on the risks from mining activities around disaster-prone and earthquake-prone areas; (ii) possible disturbance to water resources by infrastructure development in a protected forest area; (iii) potential chemical contamination from a tailing dam under consideration; (iv) social pressure on local communities caused by the influx of external workers; (v) likely air pollution; (vi) perceived heavy road traffic; and (vii) absence of an environment impact assessment for the mine extraction phase; additional concerns were identified in the CAO Assessment Report, such as fear of reprisals and safety issues related to an explosives storage facility.

12. The Complaint stated that IFC is actively exposed to DPM through equity investments in RBI and PSBC. The Complaint claimed that RBI has both equity and debt investments in Bumi Resources (BR), an Indonesian mining company, which owns a 35.73% equity stake in Bumi Resources Minerals (BRM). BRM in turn owns a 49% equity stake in DPM. The Complaint also alleged that PSBC had substantial debt investments in China Nonferrous Metal Mining (Group) Co., Ltd (CNMC), through its participation in arrangement of two perpetual medium-term note (MTN) issues for CNMC in October and November 2018. CNMC is the largest shareholder at a 33.75% equity stake of China Nonferrous Metal Industry’s Foreign Engineering and Construction Co., Ltd (NFC), which in turn owns a 51% equity stake in DPM.

13. On March 25, 2020, CAO determined that the Complaint met CAO’s eligibility criteria concerning PSBC, but not concerning RBI, whose potential exposure to DPM was determined to be immaterial. CAO’s eligibility decision appeared to hinge on the assumption that “PSBC may
have a debt exposure to CNMC and NFC.”2 This differs from the Complaint’s alleged link based on PSBC’s arrangement for the two MTNs issued by CNMC.

14. CAO provided IFC with a redacted version of the Complaint on September 18, 2021. The Complainants had originally requested that their identities be kept confidential due to concerns for personal security, although some later gave CAO permission to disclose their identities to the public. Given the lack of relationship, neither IFC nor PSBC have had any communications with the Complainants.

15. CAO released its Assessment Report on January 19, 2022. Because consensus on engaging in a voluntary dispute resolution process to address the Complaint was not achieved among the Complainants, DPM and PSBC, the Complaint was referred to CAO Compliance for appraisal at the request of the Complainants, per CAO’s Policy.

IV. MANAGEMENT RESPONSE

Coordination by IFC Pertaining to the Complaint

16. IFC was informed by CAO of the Complaint on November 22, 2019 and has since then coordinated with both CAO and PSBC to facilitate the information exchange and to address obstacles created by confidentiality concerns, as well as other challenges that arose during the process. CAO shared a diagram (Figure 1) with IFC on December 21, 2019 showing the Complaint’s claimed link between IFC and DPM through PSBC as an underwriter and potential investor in two MTNs issued by CNMC. Based on publicly available information, at the time of receiving the Complaint, the DPM mine was in a pre-construction phase.

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2 CAO eligibility decision memo to IFC concerning complaint regarding PT Dairi Prima Mineral in Indonesia, March 25, 2020. According to CAO, its eligibility assessment regarding complaints related to an IFC Financial intermediary (FI) client “weighs up various aspects to understand whether IFC has a material exposure to the project subject to a CAO complaint. Specifically, CAO considers (a) the nature of IFC’s FI investment; (b) the link between the FI and the project subject to a CAO complaint; (c) the type of exposure between the FI and the project subject to a CAO complaint; (d) the amount and tenor of the FI’s exposure to the project subject to a CAO complaint; and (e) the severity of harm or potential harm raised in the complaint.”
17. In January 2020, CAO requested specific information from PSBC via IFC on: (i) whether PSBC was an investor or arranger for the two MTNs issued by CNMC; and (ii) details of all loans that PSBC might have extended to CNMC and its subsidiaries. On February 12, 2020, through IFC and requesting information confidentiality, PSBC provided CAO with a list of historical and outstanding loans it had made to CNMC and its subsidiaries. PSBC stated that it had neither invested in nor distributed the subject two MTNs, and that all PSBC loans to CNMC and its subsidiaries were short-term working capital with tenor of no more than one year, with a defined use of proceeds in China, and unrelated to DPM.

18. On March 25, 2020, IFC was notified by CAO that the Complaint was determined eligible for assessment in relation to IFC’s investment in PSBC. IFC assisted in the establishment of a direct communication channel between CAO and PSBC. PSBC, directly and indirectly via IFC, reiterated its position to CAO that it has no financial exposure to DPM.

**ICF’s View of the Two Alleged Links between IFC and DPM via (1) the MTNs Issued by CNMC and (2) PSBC’s Short-Term Loans to CNMC and NFC**

19. Management believes that there is no factual basis of the Complaint which states that PSBC had substantial debt investments in CNMC via two MTNs, and thus for the alleged financial and active exposure of IFC to DPM. In two letters addressed to IFC dated January 14, 2020 and January 20, 2020, PSBC confirmed that although its name was included in the underwriting syndicate list in the prospectuses for CNMC’s 2018 II and III MTNs, it did not underwrite or invest in either of the subject MTNs. PSBC further explained that each MTN issued at the national interbank bond market can invite any institution who has a qualified syndicate membership in the interbank bond market to join the underwriting syndicate, and that the institution who accepts to join the underwriting syndicate will be entitled, but not obliged, to subscribe to the MTNs in the book building process. This is corroborated by the disclosed subscription instructions of the subject two MTNs showing that each underwriting syndicate

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3 https://www.chinamoney.com.cn/dqs/cm-s-notice-query/fileDownload.do?mode=open&contentId=1179246&priority=0&ut=fbmjrGQX9zE%2B1XSxdEiTEOzrB8oWpwGohoVGCliCrKlDXziyLT7e8Pn1tXBGEL3zg8t8zWKrdFd%0Ae2CR7GJDh%0A1zvQ1RhYek6X9SS92zkKrMD1RXBmsav9RykQRUR/gFys2n4t4FwwAfKyoWboqpy%0A86EnT%2BbyUYYWVW5mFL0=%0A&sign=Q/d8so1IMh3GooM15WmGuaZAJukCpO5sMwap9ByMZth4tsJZeSk3x6Wq1v31RrKsnQLCwDaAPm00%0ALsYa5AcTzc2CuvK8xTKL5JKaAphGi1EbpsADAhjeg2dCZIBVMUOFd2LaiLvRJjML9AfJTc%0A44XV2MvFkyvEBuTLsA=%0A
https://www.chinamoney.com.cn/dqs/cm-s-notice-query/fileDownload.do?mode=open&contentId=1201746&priority=0&ut=bvwl1v1GM4wPhfhiFlk7/EqycipCLy6
member’s minimum subscription amount is zero. Moreover, the China National Association of Financial Market Institutional Investors (NAFMII), which is the Self-regulatory Organization (SRO)\(^4\) overseeing MTN practices under the guidance of the People’s Bank of China, has in place the *Intermediary Service Guidelines for Debt Financing Instruments of Non-financial Enterprises in the Interbank Bond Market* (effective from April 15, 2008 and revised on April 30, 2020) and the *Syndicate Agreement Sample for Debt Financing Instruments of Non-financial Enterprises in the Interbank Bond Market* (effective from September 2, 2013). These guidelines stipulate that in order to participate in the book building process, the underwriting syndicate member has to deliver a valid subscription offer to the lead underwriter, who takes the responsibility of due diligence, organization of book building and allocation for the debt financing instruments. In this context, PSBC has confirmed that it did not deliver any subscription offer during the book building process of the two subject MTNs.

20. **Furthermore, Management understands that under the laws of the PRC and the regulations of the China Banking and Insurance Regulatory Commission (CBIRC), PSBC’s working capital loans to CNMC and NFC cannot be used to finance a long-term investment such as DPM, and hence such short-term working capital loans do not substantiate the allegation of a financial connection between IFC and DPM.** PSBC’s letter to IFC, dated May 27, 2021, confirmed that all financings from PSBC to CNMC and NFC, as designated in legal documents, have been working capital loans. As a commercial bank established under the laws of PRC, PSBC’s working capital loans are subject to the *PRC Law on Commercial Banks* (effective from July 1, 1995) and the *Interim Administrative Rules on Working Capital Loans* (effective from February 12, 2010) (Working Capital Loan Rules). Pursuant to the PRC law in general and the Working Capital Loan Rules in particular, the proceeds of a working capital loan from a PRC bank must be used by the borrower for working capital with respect to its daily production and operation needs (e.g., for inventory and operating expenses) and shall not be used by the borrower for fixed assets, equity, or capital investment in another enterprise. In line with this legal framework, PSBC

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\(^4\) NAFMII was founded in 2007 under the approval of the State Council of China. NAFMII aims to propel the development of China OTC financial market, including the interbank bond market, with the power to set industry standards and guidelines.
further confirmed in the letter that (i) these working capital loans are short-term in nature and may be used only for operating expenses and working capital purposes; (ii) the working capital loans are required to be used by the borrower in compliance with the CBIRC regulations and may not be used for fixed assets, equity, or capital investment such as overseas investment in DPM; and (iii) as of the date of the letter, PSBC has no outstanding loans with either CNMC or NFC. Additionally, NFC, as an equity investor in DPM, confirmed PSBC’s position above by providing a letter to PSBC stating that none of the loans it received from PSBC have been used for purposes related to the DPM zinc and lead mine. The NFC letter, dated May 26, 2021, has been forwarded to CAO by IFC. Given such, IFC’s understanding of the situation is shown in Figure 2. Therefore, Management is of the view that it is not possible for CNMC or NFC to bypass the legal and regulatory requirements to (a) grant the PSBC working capital loan proceeds to a subsidiary or affiliate or (b) use the working capital loan proceeds for investment in an enterprise outside of China (e.g., the DPM mine in Indonesia).

V. CONCLUSION

21. IFC takes seriously allegations regarding the E&S risks and impacts of IFC investments and is concerned about the allegations raised by the Complainants related to the mine in Indonesia. However, Management holds the view, based on substantive information obtained from PSBC and other sources to date, that there is not, nor could there have been, a financial link between IFC’s client, PSBC, and DPM. Given the lack of PSBC financial exposure to DPM, PSBC cannot be expected to require DPM to apply IFC E&S requirements, and that any alleged E&S risks and potential impacts related to DPM cannot be plausibly linked to PSBC, IFC, or any potential IFC non-compliance with E&S Policies. It is therefore IFC’s view that this Complaint does not satisfy CAO’s appraisal criteria for investigation that the alleged harm should be plausibly linked to potential IFC non-compliance. Notwithstanding the above, Management respects CAO’s process in its assessment of the Complaint in relation to IFC’s investment in PSBC and will continue to cooperate with CAO during its compliance appraisal.
DISCLAIMER

The IFC Management Response is provided in response to the Assessment Report of the Office of the Compliance Advisor Ombudsman (CAO) relating to complaints of alleged non-compliance by IFC with its Performance Standards on Environmental and Social Sustainability in a project supported by IFC finance or investment.

The CAO administers IFC’s accountability mechanism in order to address complaints by people affected by IFC supported projects. As noted in paragraph 9 of the IFC/MIGA Independent Accountability Mechanism (CAO) Policy, CAO has no authority with respect to judicial processes. CAO is not a judicial or legal enforcement mechanism, nor is CAO a substitute for courts or regulatory processes, and CAO’s analyses, conclusions, and reports are not intended or designed to be used in judicial or regulatory proceedings or for purposes of attributing legal fault or liability.

Nothing contained in the CAO's Assessment Report or in the IFC Management Response (1) creates any legal duty, (2) asserts or waives any legal position, (3) determines any legal responsibility, liability or wrongdoing, (4) constitutes an acknowledgment or acceptance of any factual circumstance or evidence of any mistake or wrongdoing, or (5) constitute any waiver of any of IFC's rights, privileges or immunities under its Articles of Agreement, international conventions or any other applicable law. IFC expressly reserves all rights.

While reasonable efforts have been made to determine that the information contained in the reports is accurate, no representation or warranty is given as to the accuracy or completeness of such information. In preparing the Management Response, IFC does not intend to create, accept or assume any legal obligation or duty, or to identify or accept any allegation of breach of any legal obligation or duty. No part of the CAO’s Assessment Report or IFC’s Management Response may be used or referred to in any judicial, arbitral, regulatory or other process without IFC’s express written consent.
CLIENT RESPONSE

Regarding

Concerns in Relation to IFC’s Investment (#35461)

February 11, 2022
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<td>BR</td>
<td>Bumi Resources</td>
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<td>BRM</td>
<td>Bumi Resources Minerals</td>
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<td>CAO</td>
<td>Office of the Compliance Advisor Ombudsman (IFC/MIGA)</td>
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<td>CNMC</td>
<td>China Nonferrous Metal Mining (Group) Co.</td>
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<td>DPM</td>
<td>Dairi Prima Mineral</td>
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<td>EPC</td>
<td>Engineering, Procurement and Construction</td>
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<tr>
<td>ESMS</td>
<td>Environmental and Social Management System</td>
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<tr>
<td>FI</td>
<td>Financial Intermediary</td>
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<tr>
<td>IFC</td>
<td>International Finance Corporation</td>
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<tr>
<td>MIGA</td>
<td>Multilateral Investment Guarantee Agency</td>
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<td>NFC</td>
<td>China Nonferrous Metal Industry's Foreign Engineering and Construction Co.</td>
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<td>NFC Hong Kong</td>
<td>NFC (Hong Kong) Metal Resources Company Limited</td>
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<td>NFC Mauritius</td>
<td>NFC (Mauritius) Mining Company Limited</td>
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<tr>
<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
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<td>OHCHR</td>
<td>Office of the United Nations High Commissioner for Human Rights</td>
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<td>Postal Savings Bank of China</td>
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A. After learning of the complaint against Dairi Prima Mineral ("DPM"), PSBC attached great importance to it and fully cooperated with CAO and IFC.

1. PSBC first learned of the complaint from IFC at the end of 2019. According to IFC’s requests, PSBC verified its financing activities with China Nonferrous Metal Mining (Group) Co. ("CNMC") and China Nonferrous Metal Industry's Foreign Engineering and Construction ("NFC"), including "how PSBC participated in or involved in these notes" and "whether PSBC owned/provided these notes/bonds or loans".

2. PSBC tried its best to contact CNMC and NFC, verifying its business relationship with CNMC and NFC. In the meanwhile, PSBC further confirmed with NFC about its relationship with DPM.

3. It was not until September 18, 2021 did PSBC receive the Complaint from CAO for the first time. PSBC immediately and carefully analyzed concerns raised by the complainants.

4. During this period, PSBC responded to the inquiries from CAO and IFC in a timely manner, providing relevant information and materials.

B. After verification, PSBC found that DPM is far beyond its leverage. The allegations regarding PSBC in the Complaint were totally based on an absolute misunderstanding of facts.

5. After reviewing the Complaint, PSBC found that complainants’ reasons for PSBC’s linkage with DPM were entirely based on their erroneous understanding of public information. Complainants mistakenly believe that PSBC underwrote CNMC’s medium-term notes. Complainants state that:

(1) In October and November of 2018, PSBC co-arranged two perpetual medium-term note issues worth $721 million for CNMC. In prospectuses accessed through the Bloomberg terminal, CNMC disclosed that it would use the capital from the issues to
fund the operations of its subsidiaries. This would put NFC and DPM squarely within the stated use of proceeds for the debt issues.1

(2) Medium-term notes are debt instruments that create continuous active material exposure between the arranger, in this case PSBC, and the issuer, in this case CNMC.2 PSBC has established an equity-like relationship with CNMC by participating in perpetual medium-term notes.3 The CAO should not apply its reasoned decision on bonds – which are debt – to an instrument that is classified as equity-like.4

(3) By underwriting two CNMC medium-term notes, whose proceeds are to be directed to the operations of its subsidiaries, PSBC is directly linked with the potential impacts of the DPM project. The OECD guidance notes that a bank that is directly linked “has a responsibility to seek to prevent or mitigate the impact, using its leverage, which may involve efforts to influence the client to provide remediation.” Therefore, PSBC has a responsibility – and the necessary leverage – to engage with CNMC over the social and environmental risks of DPM.5

6. In fact, unlike the complainants’ assertion, PSBC did not underwrite CNMC notes. PSBC’s “leverage” over CNMC, which was claimed by the complainants, did not exist:

(1) PSBC was not the lead underwriter of the 2018 II and III medium-term notes of CNMC, did not participate in the underwriting or distribution of such notes, and did not submit any Subscription Order.

(2) It is an industry practice for the issuer to invite other qualified institutions, in addition to the lead underwriter and joint lead underwriter, to participate in the distribution of such medium-term notes. Invitations were sent randomly to major financial institutions. All qualified institutions invited may be included in the list of syndicate members. Moreover, institutions who had participated before might still be kept on

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2 Id. at 8.
3 Id. at 19-20.
4 Id. at 20.
5 Id. at 20.
the list. It is obvious that those invited or listed institutions do not necessarily sell or distribute the notes, as was the case for PSBC in this instance.

(3) According to the *Intermediary Service Guidelines for Debt Financing Instruments of Non-financial Enterprises in the Interbank Bond Market* (revised on April 30, 2020) stipulated by the China National Association of Financial Market Institutional Investors, it is the lead underwriter’s duty to conduct due diligence, evaluate performance of enterprises, and set out recommending standards. Only the lead underwriter has the “leverage”. As an invited syndicate member, PSBC has neither duty nor leverage over CNMC.

7. It is apparent that the basis for the complainants’ allegation of PSBC’s financial linkage to DPM were an incorrect comprehension of facts. In fact, after verification, PSBC finds that all of its connections with CNMC and NFC are limited to short-term operational loans. According to PSBC’s management policies, CNMC and NFC can only apply for short-term operational loans rather than project loans and fixed asset loans. PSBC has a series of measures controlling the application, underwriting, and monitoring of loans. More importantly, these loans had all been **fully repaid**. PSBC had made comprehensive and truthful explanations to IFC and CAO.

8. The complainants later changed their reasons for PSBC’s financial exposure with DPM based on the feedback information provided by PSBC to CAO on the draft assessment report, stating that the loan provided by PSBC "supports NFC’s general operations, including its role as EPC contractor for the mine" which is also totally inconsistent with the facts.


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10. It is explicitly stipulated in Article 9 of Provisional Measures on Administration of Short-term operational loans that “short-term operational loans shall not be used for investments in fixed assets or equity”.

11. PSBC further confirmed through inquiries that CNMC and NFC did not use loans obtained from PSBC on DPM:

(1) On July 9, 2020, upon PSBC’s inquiry, NFC provided a statement titled PSBC’s FINANCING NOT INVOLVING DPM to PSBC, stating that “All debt financing from PSBC to CNMC and NFC are used in compliance with the requirements of China’s banking regulator. All debt financing from PSBC to NFC and all funds provided by CNMC to NFC are not used for the zinc & lead mine of DPM.”

(2) On May 26, 2021, upon PSBC’s inquiry, NFC provided a statement to PSBC stating that all financings from PSBC to NFC “have been 'short-term operational loans’ as defined by the China Banking and Insurance Regulatory Commission (CBIRC) and used only for operating expenses and working capital purposes and not for financing fixed assets or equity or capital investment. None of the loan proceeds provided by PSBC to NFC have been used for purposes relating to” DPM “zinc and lead mine in North Sumatra, Indonesia.”

12. Although PSBC is very sympathetic to concerns raised by the complainants, but PSBC, a creditor providing short-term operational loans, has no reason to hold so-called “necessary leverage” over DPM, an oversea project operated by the Client’s multi-tier oversea subsidiaries.

13. PSBC thoroughly read all the concerns raised by the Complaint with reference to IFC Performance Standards, which, according to the Complaint, applies to DPM. However, PSBC thinks that DPM, as a project in Indonesia and a third-tier subsidiary of PSBC’s short-term operational loan customer, is totally irrelevant to NFC’s use of proceeds from PSBC, thus is beyond the scope of IFC’s E&S policies.
C. DPM does not fall within "Sub-Client" or "Sub-Project" defined by CAO Policy, nor is it governed by IFC's E&S policies, not to mention IFC Performance Standards.

14. PSBC carefully reviewed its Environmental and Social Management System (“ESMS”), and had in-depth discussions with IFC on policy requirements.

15. First, it is apparent that according to CAO Policy, DPM is not a "Sub-Client" or "Sub-Project". CAO Policy defines "Sub-Client" as a "business directly supported by an FI Client that is within the use of proceeds requirements in IFC’s finance or investment documents" or MIGA’s contract of guarantee", and defines "Sub-Project" as a "business operation of a Sub-Client within the use of proceeds requirements in IFC’s finance or investment documents or MIGA’s contract of guarantee."

16. Second, according to paragraph 5, paragraph 8, footnote 6 and footnote 10 of Interpretation Note on Financial Intermediaries (“Interpretation Note”), IFC has E&S requirements on Financial Intermediaries' (“FI”) ‘lending’ (e.g., for banking institutions) and ‘investment’ (e.g., for PE Funds)” which refer to “the transactions between the FI and its clients (sub-project level for IFC)”.

17. Since IFC’s policies only govern “transactions between the FI and its clients”, therefore only PSBC’s provision of short-term operational loans to CNMC and NFC could be governed by IFC’s policies. PSBC has adopted a series of E&S controlling measures, which are fully in compliance with IFC’s E&S requirements, on its clients - CNMC and NFC. However, CNMC’s, NFC’s or their affiliates’ participation in projects outside the use of proceeds from PSBC are beyond the scope of application of IFC’s policies.

18. DPM is a fourth-tier subsidiary of CNMC and a third-tier subsidiary of NFC. More importantly, as an Indonesian company, DPM cannot possibly establish any linkage with the short-term operational loan provided by PSBC’s Beijing branch to NFC within China. DPM is not a “business directly supported by” PSBC “that is within the use of proceeds requirements in IFC’s finance or investment documents or MIGA’s contract of guarantee.” Neither does the project operated by DPM constitutes a “Sub-Client” or a “Sub-Project”.


19. It is also apparently erroneous to allege that \textit{IFC Performance Standards} applies to DPM.\footnote{Id. at 7. Complainants claimed that “PSBC, through its Environmental and Social Management System (ESMS), should have required its customer NFC, to apply the IFC Performance Standards to projects such as DPM, and noted that working capital loans are not excluded from the application of the Performance Standards.”} Paragraph 1 of \textit{Interpretation Note} regulates that “A key aspect of IFC’s approach to E&S risk management in the FI sector is to ensure that where FIs provide \textbf{project or long-term (over 36 months) corporate finance} to a borrower/investee to support a business activity that \textbf{may include} a) involuntary resettlement, b) risk of adverse impacts on Indigenous Peoples, c) significant risks to or impacts on the environment, community health and safety, biodiversity, cultural heritage or d) significant Occupational Health and Safety risks (collectively, Higher Risk transactions), the FI will appropriately assess and require its clients to mitigate these risks and impacts in line with the IFC Performance Standards.”

20. In the current case, PSBC's short-term operational loans to CNMC and NFC are neither "project finance" nor "long-term (over 36 months) corporate finance", and do not involve "high-risk activities". In such a situation, there is no basis for applying the above-mentioned policies. We have reiterated that DPM is not a "Sub-Project" defined by \textit{CAO Policy}. On the other hand, paragraph 12 of \textit{Interpretation Note} only requires that "The level and scope of Performance Standards application at the subproject level will vary depending on the FIs' level of leverage and access to information." Therefore, even if there exists a "Sub-Project" applying \textit{IFC Performance Standards} (which is not the case here), the application of \textit{IFC Performance Standards} is also decided by “FIs' level of leverage and access to information”. As mentioned above, PSBC does not have such "leverage" since it only provided short-term operational loans to CNMC and NFC.

21. PSBC has comprehensively studied CAO's precedents involving FIs. PSBC found that CAO has been cautious in recognizing a FI’s linkage to the impacts alleged by a Complaint and only initiate compliance investigation when the impacts complained possess such an imminent linkage with FI’s products or services. For example:

(1) In \textit{India: India Infrastructure Fund-01/Dhenkanal District}, the FI client (India Infrastructure Fund) invested for a thermal coal-based power plant.\footnote{\textit{CAO Appraisal for Compliance Investigation of IFC 9}, available at \url{https://www.cao-ombudsman.org/sites/default/files/downloads/CAO_Appraisal_IndiaInfrastructureFund_June262013.pdf}.}
(2) In Guatemala: **CIFI-01/ Hidro Santa Cruz**, the FI client (Corporación Interamericana para el Financiamiento de Infraestructura, S.A.) made a debt and quasi-equity investment in Hidro Santa Cruz, S.A to support the development of a 5 megawatts run-of-river hydropower plant.9

(3) In **Philippines: Rizal Commercial Banking Corporation (RCBC)-01**, the FI client (Rizal Commercial Banking Corporation) financed 11 coal fired power plants.10

(4) In Guatemala: **Real LRIF-01/Coban**, the FI client (Latin Renewables Infrastructure Fund LP) invested in the Santa Rita Hydroelectric Power Plant.11

(5) In **Honduras: Ficohsa-02/Tela**, the FI client (Banco Financiera Comercial Hondureña, S.A.) organized a syndicated loan of US$24 million (with US$10 million provided by the FI client) to support the project of Indura Beach and Golf Resort.12

22. In no case did CAO decide to investigate when the FI was alleged to have an immaterial linkage as PSBC has in this case.

23. PSBC also reviewed the policies and guidelines issued by Organization for Economic Cooperation and Development (“OECD”), whose policies were cited in the Complaint, and United Nations High Commissioner for Human Rights (“OHCHR”), whose policies were referenced in relevant OECD policies. Referring to regulations made by OHCHR and OECD, there also exist no linkage between PSBC and DPM.

(1) OECD’s **Due Diligence for Responsible Corporate Lending and Securities Underwriting**13 and OHCHR’s **Guiding Principles on Business and Human rights**14 and **THE CORPORATE RESPONSIBILITY TO RESPECT HUMAN RIGHTS**15 point

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out that financial institutions could be involved in E&S impact in 3 ways: cause, contribution and direct linkage.

(2) Among those 3 ways, “direct linkage” is the weakest. Paragraph 18 of Request from the Chair of the OECD Working Party on Responsible Business Conduct\(^6\) clarified that “there is either a direct link between the adverse impact and the products or services a financial institution provides to clients or investee companies or there is no link — there is no such concepts as ‘indirect linkage’ or ‘indirect impacts’ in the Guiding Principles.”

(3) What alleged by the Complaint is also “direct linkage”. As previously mentioned in paragraph 5(3), the Complaint alleged that “the OECD guidance notes that a bank that is directly linked ‘has a responsibility to seek to prevent or mitigate the impact, using its leverage, which may involve efforts to influence the client to provide remediation’”, and therefore, PSBC “has a responsibility – and the necessary leverage – to engage with” NFC “over the social and environmental risks of” DPM.

24. Apparently, there is no such linkage between PSBC and E&S impacts alleged by the Complainants.

(1) According to OHCHR and OECD, a direct linkage requires a financial institution to have “the least direct control or influence over whether that impact occurs”\(^7\), and it “needs to be between the financial product or service provided by the bank and the adverse impact itself”\(^8\). Moreover, examples of direct linkage provided by OHCHR and OECD are all about “lending money to”\(^9\), “providing financial

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loans to"20, investing in or “managing the assets of”21 an enterprise for business activities that result in the adverse impact.

(2) OHCHR specifically points out that “the mere existence of... a business relationship does not automatically mean that there is a direct link between an adverse impact and the bank’s financial product or service”.22 Besides, “from the financial sector, an example of a situation that would be excluded from the scope of GP 13 (b) would be where a bank provides project finance to a company for a specific project, and that company is involved in adverse... impacts in activities unrelated to the project financed by the bank.”23

25. To sum up, through the business relationships between PSBC and NFC, and between PSBC and CNMC, DPM is neither governed by CAO Policy and IFC’s E&S policies, nor by IFC Performance Standards. Whether under policies of CAO and IFC, or “international good practice standards” that CAO will follow when carrying out its work according to CAO Policy24, PSBC has no linkage with complained impacts resulted by DPM.

D. PSBC is extremely confused about why CAO found the complaint to Raiffeisen Bank International (“RBI”) ineligible due to immaterial exposure, yet refused to apply the same standard on the eligibility regarding PSBC.

26. The Complaint elaborated on RBI’s financial exposure to DPM. PSBC found that RBI’s exposure is more material than PSBC’s.

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20 Supra note 17, at 17.
21 Supra note 19, at 3.
22 Supra note 18, at 6.
24 Paragraph 10 of CAO Policy stipulates that “CAO carries out its work guided by the following core principles: ...Consistency with good practice: Following international good practice standards consistent with this Policy, including the responsibility of business to respect human rights”. 
27. By research via public source, PSBC found that RBI’s exposure to DPM is more material both through the connection between IFC and its FI, and through the connection between FI, FI’s Sub-Client and DMP. Please see *ANNEX B. INFORMATION PROVIDED BY PSBC REGARDING RAFFEISEN BANK INTERNATIONAL (RBI)* of the Assessment Report \(^{25}\) for details. Those contents could be summarized by two diagrams:

![Figure 1 RBI’s financial exposure to DPM](image1.png)

![Figure 2 PSBC’s financial exposure to DPM](image2.png)

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28. Although, at the end of 2019 and the beginning of 2020, PSBC clarified its relationship with CNMC and NFC, CAO still found the Complaint on PSBC eligible in March 2020.

29. PSBC was given no chance to review the Complaint until September 18, 2021, and it was only after that time did PSBC realize that the Complaint put more emphasis on RBI. Moreover, PSBC was given no chance to learn about CAO’s decision regarding RBI’s ineligibility, until CAO sent the first draft of Assessment Report on October 28, 2021. It was only indicated in the footnote of the report that “Considering available information on RBI’s potential exposure to DPM and how it was acquired, CAO determined this not to be a material exposure with respect to CAO’s eligibility criteria”.

30. PSBC was extremely confused about why CAO found the complaint on RBI ineligible due to immaterial exposure, but declined to apply the same standard on the eligibility regarding PSBC.

31. PSBC has made utmost effort to conduct research through publicly available information, to analyze and compare the alleged link of PSBC and of RBI and made every effort to seek clarifications from CAO. On November 11, 2021, PSBC sent a letter with 10 exhibits to CAO comparing IFC’s connection with DPM through RBI and PSBC, hoping that CAO could explain why the complaint on RBI ineligible but the complaint on PSBC eligible. CAO only replied that “it would be pertinent to the compliance appraisal process”.

E. **PSBC has a well-operated ESMS which has been widely recognized.**

32. PSBC has enforced all E&S requirements under *Strategic Cooperation Agreement* where IFC agreed to provide consulting services to PSBC in multiple areas including E&S management. PSBC has always been cooperating closely with IFC to seek their advice on E&S matters.

33. PSBC has reputable E&S performance which has received high recognition. Relevant honors obtained in recent years include but not limited to:

   (1) PSBC was rated A by Morgan Stanley Capital International Inc. in its latest Environmental, Social and Governance Rating for 2021.
(2) PSBC won the Global Green Finance Innovation Award rewarded by International Finance Forum.

(3) PSBC was rewarded “Leading Institution in Evaluation of Green Banks” by China Banking Association for many years.

F. PSBC’s opinion.

34. PSBC has always put great emphasis on E&S management and will continue to improve its E&S performance. PSBC has taken all possible measures to actively cooperate with CAO and IFC.

35. PSBC has always been cooperating in good faith. After careful study and thorough discussion with IFC about their policies, PSBC thinks DPM is outside the scope of application of IFC’s E&S policies, not to mention the IFC Performance Standards. None of IFC’s policies include unreasonable requirements such as requiring a FI to exert the leverage which it could not possibly have or acquire.

36. To conclude, the Complaint does not raise any issue of non-compliance with IFC’s E&S policies. Therefore, the Complaint does not meet the criteria set in Article 91 of CAO Policy, which includes “whether there are preliminary indications that IFC/MIGA may not have complied with its E&S Policies” and “whether the alleged Harm is plausibly linked to the potential non-compliance”. PSBC respectfully requests CAO to close this case.

37. PSBC thinks finding the complaint to PSBC eligible is a waste of CAO’s valuable resources and is of no value to resolve the complainants’ concerns. In addition, at the complaint assessment stage, CAO did not explain why it found the complaint on RBI ineligible but the complaint on PSBC eligible. PSBC hopes that CAO could explain it at the compliance appraisal stage to clear up PSBC’s confusion, following the principles
stipulated in paragraph 10 of CAO Policy, i.e., being transparent, accessible, responsive, 
fair\textsuperscript{26}, equitable\textsuperscript{27}, predictable, and consistent with good practice. 

\textsuperscript{26} Paragraph 10(e) of CAO Policy stipulates that “all relevant stakeholders… are treated respectfully on fair, equitable, and informed terms.”

\textsuperscript{27} Id.
Disclaimer

This PSBC Client Response is provided in response to the Assessment Report of the Office of the Compliance Advisor Ombudsman (CAO) finding a complaint eligible for compliance appraisal.

Nothing in this PSBC Client Response or in the process provided for in the CAO Policy (“CAO Process”) (1) creates any legal duty, (2) asserts or waives any legal position, (3) determines any legal responsibility, liability, or wrongdoing, (4) constitutes an acknowledgment or acceptance of any factual circumstance or evidence of any mistake or wrongdoing, or (5) constitutes any waiver of any of PSBC’s rights, privileges, or immunities under its Articles of Agreement, international conventions, or any other applicable law. PSBC expressly reserves all rights, privileges, and immunities. PSBC does not create, accept, or assume any legal obligation or duty, or identify or accept any allegation of breach of any legal obligation or duty by virtue of this PSBC Client Response.

While reasonable efforts have been made to determine that the information contained in this PSBC Client Response is accurate, no representation or warranty is given as to the accuracy or completeness of such information.

According to paragraph 9 of CAO Policy, CAO is not a judicial or legal enforcement mechanism. Its analyses, conclusions, and reports are not intended to be used in judicial or regulatory proceedings nor to attribute legal fault or liability and it does not engage in factfinding nor determine the weight that should be afforded to any evidence or information.

No part of this PSBC Client Response or the CAO Process may be used or referred to in any judicial, arbitral, regulatory, or other process without PSBC’s express written consent.
Appendix D: Considerations Relevant to the Appraisal per CAO Policy

The CAO Policy[1] provides for the compliance appraisal to take into account additional considerations, as outlined in the table below.

<table>
<thead>
<tr>
<th>CAO Policy provision</th>
<th>Analysis for this case</th>
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<tbody>
<tr>
<td>For any Project or Sub-Project where an IFC/MIGA Exit has occurred at the time CAO completes its compliance appraisal, whether an investigation would provide particular value in terms of accountability, learning, or remedial action despite an IFC/MIGA Exit (para. 92a).</td>
<td>At the time of writing IFC had an active investment in PSBC, however PSBC did not have any active loans to CNMC or NFC. CAO considers that an investigation would not provide particular value in terms of accountability, learning or remedial action. See report body, Section 5d for further discussion.</td>
</tr>
<tr>
<td>The relevance of any concluded, pending or ongoing judicial or non-judicial proceeding regarding the subject matter of the complaint (para. 92b).</td>
<td>To CAO's knowledge there is no concluded, pending or ongoing judicial or non-judicial proceeding regarding the subject matter of the complaint (the risks and impacts of the DPM mine).</td>
</tr>
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<td>Whether Management has clearly demonstrated that it dealt appropriately with the issues raised by the Complainant or in the internal request and followed E&amp;S Policies or whether Management acknowledged that it did not comply with relevant E&amp;S Policies (para. 92c).</td>
<td>As outlined in the body of this report, there are preliminary indications of non-compliance. In this context, CAO concludes that IFC has not clearly demonstrated that it dealt appropriately with issues raised by the complaint, nor has IFC acknowledged non-compliance with relevant E&amp;S Policies.</td>
</tr>
<tr>
<td>Whether Management has provided a statement of specific remedial actions, and whether, in CAO's judgment after considering the Complainant's views, these proposed remedial actions substantively address the matters raised by the Complainant (para. 92d).</td>
<td>IFC's Management Response does not include any statements indicating plans to undertake remedial actions to address issues raised by complainants for appraisal.</td>
</tr>
<tr>
<td>In relation to a Project or Sub-Project that has already been the subject of a compliance investigation, CAO may: (a) close the complaint; (b) merge the complaint with the earlier compliance process, if still open, and the complaint is substantially related to the same issues as the earlier compliance process; or (c) initiate a new compliance investigation only where the complaint raises new issues or new evidence is available (para. 93).</td>
<td>Not applicable</td>
</tr>
</tbody>
</table>