

SOUTHEAST EUROPE EQUITY FUND II

REQUEST NUMBER: 2017/05

COMPLIANCE REVIEW REPORT – October 2018

The Project Complaint Mechanism (PCM) is the independent accountability mechanism of the EBRD. PCM provides an opportunity for an independent review of complaints from one or more individual(s) or organisation(s) concerning an EBRD project, which allegedly has caused, or is likely to cause harm. PCM may address Complaints through two functions: Compliance Review, which seeks to determine whether or not the EBRD has complied with its Environmental and Social Policy and/or the project-specific provisions of the Public Information Policy; and Problem-solving, which has the objective of restoring a dialogue between the Complainant and the Client to resolve the issue(s) underlying a Complaint without attributing blame or fault. Affected parties can request one or both of these functions.
For more information about PCM, contact us or visit www.ebrd.com.

Contact information

Inquiries should be addressed to:

The Project Complaint Mechanism (PCM)
European Bank for Reconstruction and Development
One Exchange Square
London EC2A 2JN
Telephone: +44 (0)20 7338 6000
Fax: +44 (0)20 7338 7633
Email: pcm@ebrd.com

 <http://www.ebrd.com/work-with-us/project-finance/project-complaint-mechanism.html>

How to submit a complaint to the PCM

Complaints about the environmental and social performance of the EBRD can be submitted by email, telephone or in writing at the above address, or via the online form at:

 <http://www.ebrd.com/work-with-us/project-finance/project-complaint-mechanism/submit-a-complaint.html>

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NOTE: Unless otherwise defined, capitalised terms used in this Compliance Review Report refer to terms as defined in the PCM Rules of Procedure.

Acronym List

AHK	American Hospital Kosovo (subsidiary of American Hospital)
American Hospital	American Hospital of Albania (Portfolio investment of the Fund)
BCM	Bedminster Capital Management, G.P., LLC (the initial Fund Manager)
EBRD	European Bank for Reconstruction and Development
FI	Financial Institution
OPIC	Overseas Private Investment Corporation
PCM	Project Complaint Mechanism of EBRD
RP	Rules of Procedure
SEAF	Small Enterprise Assistance Funds (the Fund Manager since May 2017)
SEC	Securities & Exchange Commission (independent US federal government agency responsible for protecting investors, maintaining fair and orderly functioning of securities markets and facilitating capital formation)
The Fund (SEEF)	Southeast Europe Equity Fund II (B) L.P
ToR	Terms of Reference

Executive Summary

The Bank's Project Complaint Mechanism (PCM) received a complaint on 7 August 2017 regarding its investment in Southeast Europe Equity Fund II (SEEF), in relation to the management of its sub-project in the American Hospital Kosovo (AHK). The Complaint alleges unfair and discriminatory treatment by management based upon grounds of nationality and further complains of a climate of fear prevailing among Kosovar employees of the Company.

The Complaint was assessed and found eligible for Compliance Review in February 2018.

Although the Complainant framed his Complaint in terms of the EBRD 2008 Environmental and Social Policy, the Bank determined that the applicable Policy should be the 2003 Environmental Policy, because this was the policy in force at the time of the signature of the Investment Agreement establishing the Fund in September 2005.

The US development agency, Overseas Private Investment Corporation (OPIC), is a co-investor in the Fund and it was agreed that environmental and social compliance due diligence and oversight would be provided by OPIC in line with its own procedures and guidelines. There is a clear coincidence of coverage between the procedures and guidelines of the EBRD and the OPIC.

The Compliance Review Expert emphasizes that it is not the task of the Compliance Review to adjudicate on an individual contract dispute at the level of the sub-project of an FI. The focus of compliance is upon the actions of the EBRD in its ongoing monitoring of its investment in the FI.

In this latter respect the Reviewer finds the EBRD to be not in compliance with requirements for ongoing monitoring under EBRD's *Environmental Procedures for Private Equity Funds*¹.

The Reviewer also notes that reliance on the 2003 Environmental Policy and Procedures for monitoring this project provides a low level of assurance in regard to the environmental and social evolution of the investment in line with the bank's current and publicly promoted aims and objectives. The Reviewer therefore urges the bank to consider Recommendations to improve its effort to monitor historical FI projects in future.

The Review recommends that the Bank address certain inconsistencies in its own Procedures and Performance Requirements that arise with projects begun at different historical junctures. The aim would be to bring all projects within a commonly understood and administered framework of compliance. This would require that investment agreements with clients contain language that foresees the need to update compliance requirements in line with changes introduced by the Bank in its occasional reviews in the pursuit of "*continuous improvement of performance management*".

¹Environmental Procedures for Private Equity Funds, Annex 8, Annual Environmental Report, (1) (a) (ii), (iii), (iv), (vi), and (b), EBRD, 2003 Edition

Introduction

(i) Project Background and Context

1. The European Bank for Reconstruction and Development (EBRD) is a Limited Partner in the Southeast Europe Equity Fund II (B) L.P. ('the Fund'), a Cayman Islands Exempted Limited Partnership. The Bank's investment in Fund was approved by the EBRD Board on 6th September 2005 and was categorised as an 'FI' investment under the 2003 Environmental Policy².
2. The Overseas Private Investment Corporation ('OPIC'), a US government agency, is a co-investor in the Fund, but is not a Partner.
3. The Fund is a "private regional equity fund seeking long-term capital appreciation through privately negotiated transactions in the equity of companies operating in Southeast Europe and neighbouring countries"³.
4. The Fund had an initial target size of US\$200 million of which the EBRD is investing US\$50 million⁴. The Fund is now estimated at approximately US\$320 million.
5. Management of the Fund was initially handled by the General Partner, SEEF GP, L.P., acting via its general partner, BCM GP, LLC⁵. BCM was replaced as General Partner and Manager of the Fund in May 2017 by Small Enterprise Assistance Funds (SEAF) ⁶- an SEC registered impact investment fund manager.
6. In 2006 the Fund invested in the American Hospital of Albania ('American Hospital'), the first private hospital in that region. In 2012, the American Hospital established a subsidiary – the American Hospital Kosovo – in Prishtina, Kosovo⁷.

(ii) Registered Complaint

7. On 2nd August 2017 the Project Complaint Mechanism (PCM) received a complaint regarding the Fund in relation to management of its holding in the American Hospital Kosovo (AHK)⁸. Both a Problem-solving Initiative and a Compliance Review were requested. The Complaint was registered in the PCM system on 18th August 2017 as Complaint number 2017/05.
8. The Complainant had previously (April 2016) filed a complaint with the OPIC Office of Accountability, since OPIC is a co-investor in the Fund. The OPIC mechanism found the complainant ineligible under its guidelines and, according to the Complainant, it advised him to refer to the EBRD PCM⁹. The substance of the

² Project Summary document 'Southeast Europe Equity Fund II', <https://www.ebrd.com/work-with-us/projects/psd/southeast-europe-equity-fund-ii.html>

³ *ibid*

⁴ *ibid*.

⁵ Amended and Restated Agreement of Limited Partnership of Southeast Europe Equity Fund II (B), L.P., A Cayman Islands Limited Partnership, dated 30th March 2006.

⁶ Interview with David Mathewson, President, SEAF, 25th April 2018 and SEAF press release of May 16th 2017 at <http://seaf.com/seaf-appointed-gp-manager-seef-fund-ii/>

⁷ *ibid*.

⁸ Eligibility Assessment Report for Compliance Review – February 2018. Request number 2017/5.

⁹ Complaint Number 2017/05 in Annex and at <https://www.ebrd.com/work-with-us/project-finance/project-complaint-mechanism/pcm-register.html>

Complaint is summarized below for sake of clarity and without prejudice to the accuracy of otherwise of the issues raised.

9. The Complainant alleges unfair treatment and discrimination when the American Hospital Board decided not to renew his service contract after the completion of four years in his role as Executive Director of AHK. The Complainant states that this was done without adequate warning or consultation and followed a period when he was prevented from fulfilling his duties by intervention from the management of the parent company in Albania.
10. The Complainant further alleges that similar unfair treatment was visited upon other Kosovar employees of AHK who, it is claimed, were terminated or downgraded by the company without justification.
11. These actions are alleged to have taken place in an atmosphere of fear and discrimination based on nationality. It is suggested that patient care also suffered and that the reputation of foreign investment in Kosovo was negatively impacted as a result of the events complained of.

(iii) Eligibility Assessment and Terms of Reference

12. In accordance with the PCM Rules of Procedure (RP), an Eligibility Assessor was appointed on 13th September 2017 to conduct an Eligibility Assessment jointly with the PCM Officer (para. 22 of PCM RPs).
 13. The Eligibility Assessors undertook a general examination of the Complaint and of additional information provided by the Complainant, the Client and by EBRD Management to determine whether the eligibility criteria for a Compliance Review were met. No site visit was considered necessary given the quality of documentation and the availability of the parties for discussion.
 14. Following this review, the Eligibility Assessors determined that the Complaint does meet the Eligibility for a Compliance Review.
 15. The Assessors indicate that the Complaint relates to relevant EBRD Policy on labour rights, decent working conditions and social standards.
 16. The Complainant framed his Complaint in terms of the EBRD 2008 Environmental and Social Policy; however, the Bank asserts that the applicable Policy is the 2003 Environmental Policy, because this was in force at the time when the Bank invested in the Project. In any case, the Assessors considered that paragraph 27(a) of the PCM RPs is satisfied, since the complaint raises matters for which the Bank had a responsibility under the 2003 Environmental Policy in relation to due diligence on the FI Project and monitoring of the Client's commitments.
 17. The ToR state that the aim of the Compliance Review is "to determine, as per PCM RP 41, if (and if so, how and why) any EBRD action, or failure to act, has resulted in non-compliance with a Relevant EBRD Policy. If it is determined that there has been non-compliance, the Compliance Review will recommend remedial changes and project monitoring, in accordance with PCM RP 41 and RP 44."
 18. The ToR (para. 8) also indicates that "The Consultant shall confine the Compliance Review to issues raised in the present Complaint. It shall not go beyond the
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parameters of the Complaint to address other issues, unless it is agreed upon by both the Consultant and the OL/PCM Officer that these issues are critical to the resolution of the Registered Complaint”.

19. Paragraph 9 of the ToR limits the Compliance Review “to reviewing actions or inactions by the EBRD in relation to the relevant policies, and does not cover any actions or inactions by the Client, (or) the Fund, managed by SEAF”.

Compliance Review Methodology

20. A full document review was undertaken by the Compliance Review Expert including all information supplied by the Complainant, responses of the Client and relevant policies and procedures of the EBRD. Staff of the Bank’s Environment and Sustainability Department were very supportive in obtaining documentation from the co-funder, OPIC, in regard to due diligence and the original funding agreement establishing the Fund. A brief desk review of the cultural, social and political interactions between Albania and Kosovo was also undertaken to contextualise the debate over discrimination.
21. Interviews were conducted for background with the PCM Office and Environmental and Sustainability staff of the Bank, as well as with the current Finance Administrator.
22. The Compliance Review Expert met via conference call with the Complainant and with a representative of the Client.
23. A brief questionnaire was sent to 11 former AHK employees whom the Complainant indicated had also suffered discriminatory treatment and harassment at AHK. The purpose of this questionnaire was to check whether the Complaint related to a single person, or to a group of persons as claimed in the substance of the Complaint. It was not in any way a retrospective employee survey of the overall state of industrial relations in AHK in 2015.
24. No site visit was undertaken on this investigation as the local personnel and situation had changed considerably since the time of the alleged events complained of and all interviews necessary were possible to pursue more easily by conference call and e-mail.

Review of Complaint

(i) Complaint Description

25. The following issues are summarised as the target of the Complaint:
 - i) That the Complainant’s labour rights were not respected by the Client;
 - ii) That the EBRD failed to promote decent work in its investment in the American Hospital;
 - iii) That the EBRD failed to ensure implementation of national and international labour law and best practice by the Client;
 - iv) That the EBRD failed to ensure that its contractor follows appropriate social standards;
 - v) That the EBRD failed to ensure that its client meets all applicable Performance Requirements.

26. The Complainant motivates these complaints by reference to the following allegations of harm caused to himself and others by the Client:
- “• Violated my human and worker rights as well as the rights of many other Kosovar colleagues
 - Misused my professional and personal integrity;
 - Discriminated Kosovar professionals by not offering them publicly a chance to apply for managerial positions at the hospital;
 - Installed fear and insecurity among Kosovar staff
 - Ruined the enormous efforts made in raising the human resources capacity of Kosovars in the health care sector.
 - Violated the objective of the investment by not working on sustainability of the project and allowing business practices that would prioritize financial interests only.”¹⁰
27. The Complainant further indicates his aim in raising the Complaint as follows:
- “I would like that lessons learned from this project are taken seriously for other projects of EBRD. For this project in particular, I would like that they try to solve whatever can be still solved and make sure this will not happen in the future for the employees of EBRD’s clients in Kosovo.”¹¹

(ii) Relevant EBRD Policy and Performance Requirements

28. The public Project Summary document¹² states “The Fund will follow the EBRD’s Environmental Procedures for Private Equity Funds. In implementing these procedures, the Fund will assess potential environmental issues associated with its investments which are required to comply, at a minimum, with local/national, health, safety, labour, environmental and public consultation requirements.”
29. In order to undertake this assessment process, however, a subsequent minute of the EBRD Board¹³ indicates: “Given the involvement of OPIC, the Fund Manager has agreed to implement environmental due diligence procedures according to OPIC requirements and adhere to a joint EBRD/OPIC environmental exclusion list. The Fund will submit Annual Environmental Reports to both investors.”
30. The Partnership Agreement¹⁴ refers to ‘Investment Guidelines’ that are appended to the agreement as Exhibit II and that will guide the investment activities of the Fund. Those guidelines in turn refer to OPIC policies in regard to its Consent for Investments in Portfolio Companies. In its second paragraph on ‘Review Procedures’ the Guideline document states: “In connection with the issuance of a Consent Notice, OPIC’s review of a proposed Portfolio Investment shall not encompass the investment merits of the proposed Portfolio Investment but will be limited to determining compliance of the proposed Portfolio Investment with OPIC’s statutory requirements, board resolutions and policies including, without limitation, *environmental policies, US economic impact policies, worker rights policies, and human rights policies.*” (Underline added).

¹⁰ Complaint.

¹¹ *ibid*

¹² Project Summary see footnote 1 above

¹³ EBRD Board document 22nd August 2005, page 18, Section 3.3 *Environment*

¹⁴ See footnote 4 above, para 2.6.

31. The text of the Partnership Agreement para. 2.6 continues: “The Investment Guidelines of the Partnership may be changed with the unanimous consent of the Advisory Committee and the prior written consent of OPIC...” There is no record of any change being requested to the Investment Guidelines.
32. Article 4 of the Partnership Agreement deals with the subject of Management of the Fund and para. (b) emphasizes that no Partner, other than the general Partner (initially Bedminster Capital Management, later SEAF) “*shall take part in the conduct or have any control over the partnership’s business*”. Article 4 (e) does, however, state “*The Partnership and the general partner (to the extent of its obligations hereunder) shall comply with any obligations it has to OPIC*”.
33. Article 5.5 of the Partnership Agreement, titled ‘Environmental Matters’, states: “EBRD will receive copies of any consents provided by OPIC to the Fund with respect to the Fund’s investments in Portfolio Companies. The Partnership will provide EBRD with the Annual Environmental Report”. Article 9.1 (b) (iv) indicates that this report shall be delivered to the EBRD within 90 days after the end of each fiscal year.
34. In addition, Article 9.1 (b) (ix) requires the General Partner to use its commercially reasonable efforts to furnish to the EBRD “*such information as EBRD may reasonably request from time to time, including information in order to monitor the compliance of the fund and its Portfolio Companies with the Investment Guidelines and the Environmental Procedures*”.
35. Exhibit III of the Partnership Agreement is the ‘Environmental Exclusion List’ showing the joint OPIC/EBRD Categorical Prohibitions that the Fund shall not finance. Paragraphs IX of that document excludes investments in countries that are ineligible for OPIC support based upon US trade and GSP categorizations. Paragraph X covers “*Investments in which the fund does not agree to ensure (or if a minority investor, make all reasonable efforts to ensure) that the portfolio company does not interfere with the rights of association, organization or collective bargaining, does not use forced or compulsory labour and observes applicable laws with respect to minimum age, hours of work and acceptable working conditions with respect to the minimum wage, hours of work and occupational health and safety*”. There is no specific identification of discrimination or general treatment of employees at the level of the enterprise as grounds for exclusion within this document.
36. The impact of these clauses is to place the emphasis for due diligence and compliance upon OPIC and against OPIC requirements, with the EBRD in a position to receive information and to conduct such monitoring as appropriate to ensure that the Fund meets and continues to meet EBRD investment criteria. This does not free the EBRD from any responsibility to ensure that the procedures used in OPIC’s assessment and compliance monitoring provide information and safeguards sufficient for EBRD to monitor and to meet its obligations in terms of its own standards and guidelines. In effect, it outsources the performance of necessary due diligence to the OPIC apparatus to reduce duplication of effort and to husband scarce resources¹⁵.
37. The Complainant uses the 2008 Environmental and Social Policy of the EBRD as his reference for the Complaint and quotes the relevant paragraphs from that document in support of his submission. However, the Bank has asserted that the

¹⁵ Interview with EBRD Environmental and Sustainability staff, 26th March 2018

relevant Policy is the Environmental Policy of 2003, because that was the Policy in force at the time of the initial investment in the Fund in 2005¹⁶. This is in line with the EBRDs Environmental and Social Procedures 2010 that state, in para 3: *“All potential projects proceeding to the initial stage of approval (currently termed Concept Review for investment operations and TC Review Committee review for technical assistance projects) after 12 November 2008 will be governed by the ESP and these Procedures. All earlier projects under consideration and approved projects will continue to be governed by the EBRDs 1996 or 2003 Environmental Policy and Procedures, as applicable at the time of project approval by the Board of Directors...”*¹⁷ and with the EBRD’s most current Environmental and Social Policy of 2014 that carries the fore note *“The current Policy and Related Performance Requirements...will apply to projects that are initiated after 7 November 2014.”*¹⁸

38. The EBRDs Environmental Policy 2003 defines the word ‘environmental’ very broadly, in the following words: *“In line with its mandate to promote environmentally sound and sustainable development, the term “environment” is used in this Policy in a broad sense to incorporate not only ecological aspects but also worker protection issues (these include occupational health and safety, harmful child labour, forced labour and discriminatory practices) and community issues, such as cultural property, involuntary resettlement, and impacts on indigenous peoples.”*
39. In its opening Mission Statement, OPIC’s Environmental Handbook of 2004 (the relevant reference at the time of signing the Partnership Agreement) states *“OPIC will assure that the projects it supports are consistent with sound environmental and worker rights standards. In conducting its programs, OPIC will also take into account guidance from the Administration and Congress on a country’s observance of, and respect for, human rights.”* There is, therefore, a strong coherence between the sets of criteria used by the two institutions for purposes of environmental and social assessment.
40. The Bank’s *‘Environmental Procedures for Private Equity Funds’*¹⁹ require the Fund to meet the following requirements:
 - “The Fund will conduct its activities with due regard to environmental factors and the principles of environmentally sound and sustainable development
 - The Fund’s investment strategy must comply with the Bank’s FI Environmental Exclusion and Referral List
 - Companies in which the Fund invests shall comply, at a minimum, with the health, safety, worker protection and environmental regulations and standards applicable in the country where the investment is situated
 - The Fund will report periodically to EBRD on the environmental performance of investments
 - The Manager of the fund will have overall responsibility for environmental risk management and implementation of these procedures within the Fund.”

Annex 8 to the Procedures also sets forth specific requirements for the content and coverage of Annual Environmental Reports to the Bank by the Fund.

¹⁶ Eligibility Assessment (see above) and interview with EBRD Environmental and Sustainability staff of 26th March 2018.

¹⁷ Environmental and Social Procedures 2010, Introduction paragraph 3, EBRD.

¹⁸ Environmental and Social Policy, May 2014.

¹⁹ Environmental Procedures for Private Equity Funds, EBRD, 2003.

(iii) Responses to the Complaint

Complaint (a)

41. *That the Complainant's labour rights were not respected by the Client in regard to the termination of his contract and the removal of his executive power before his due date of departure*

Complainant's position

The Complainant states that on 15 August 2015 the Board of American Hospitals, unilaterally and without prior consultation with the Complainant, changed his responsibilities from that of Executive Director of AHK to that of Executive Director of a 'non-existent' Hospital for Invasive Cardiology and Cardio-surgery without amending his existing Management Agreement with the company. His protests to the Board of American Hospital were ignored.

42. The Complainant further claims that at that time he was prevented from handing over his responsibilities and duties for operations, finance and human resources to the newly appointed Executive Director of the AHK while the entire management team of AHK was replaced. All the new members of the management team were of Albanian, not Kosovar, origin.
43. Again, on 31 August 2015, the Complainant's position was changed without prior consultation – this time to that of Executive Director for Business Development and Public Relations. At this point his duties as Executive Director were removed from him and he was placed in a position of being an impotent witness to the expulsion or downgrading of several co-workers from their jobs by the new Executive Director. He notes that his protests to the American Hospital Board went unanswered.
44. On 1st October 2015 he was informed that his contract with the company would not be renewed when it expired at term on 1st January 2016.
45. The Complainant has since filed a civil case in the Basic Court of Pristina on the grounds not of discrimination, but for non-fulfilment of contract and material and non-material damages against American Hospital. The case is still sub judice and is defended by the company.

Client Response

46. The client rejects all these allegations as baseless²⁰. Although it was not possible to interview a representative of the Client who had been in post at the time of the events complained of, an interview was conducted with a representative who had been a key executive of the BCM until 2009 and is now an executive of the SEAF since 2017. He pointed out that the Board of the Company had taken a formal business decision in September 2015 not to renew the contract of the complainant at its natural expiry date and had given adequate and legally sufficient notice of that decision²¹. The notice period provided for in the employment contract with the Complainant was fully complied with and gave no requirement for prior consultation between the parties. It was only when the Complainant refused to accept an initial notification that his contract would not be renewed that the Company invoked the formal termination procedure²².

²⁰ Statement of Southeast Europe Equity Fund II dated 5th October 2017 and interview with a representative of the Client by conference call on 25th April 2018.

²¹ Resolution of the Management Board of SEEF dated 25th September 2015

²² Client's comment to Review draft of 12th July 2018

47. The Management Agreement with the Complainant did not require any reason to be given for non-renewal at the natural conclusion of its term²³. The company would be defending its position very strongly in the courts.

The Bank's Response

48. Staff of the Environmental and Sustainability Department of EBRD pointed out that the Bank had relied upon the OPIC procedures and monitoring system to oversee compliance of this investment, as per decision of the Bank's Board of Directors.
49. It was confirmed that the EBRD had no direct interaction with sub-projects of the FI in line with policy. The 2003 Environmental Policy defines investment appraisal and monitoring procedures for portfolio investments as the responsibility of the FI²⁴. Some 40 per cent of the EBRD's activity was said to be in FI investments. No field contact or direct monitoring activity was undertaken in this case, as it was deemed not necessary since no other negative information had been received and resources were very limited at the Bank for this work.²⁵

Observations

50. EBRD's Environmental Policy 2003 points out that where EBRD financing is an equity investment, the Bank's environmental requirements will apply to the entire portfolio and it states²⁶ *"The FI will require sub-projects to comply, at a minimum, with the environmental regulations and standards ...of the country where the sub-project is located"*. Recalling the wide interpretation of the term 'environmental' mentioned in para 39 above, the application of national employment law is clearly relevant.
51. The purpose of this present Compliance Review is not, in any case, to determine compliance or non-compliance by the Client or the Portfolio Company. It is to determine whether the EBRD was in compliance with its own environmental policies and procedures in agreeing, monitoring and continuing to invest in the Fund.
52. The Partnership Agreement²⁷ governing this Project states that "The General Partner, in its discretion, is authorized to employ, engage and dismiss (with or without cause), on behalf of the Partnership, any Person, including an Affiliate of any Partner, to perform services for, or furnish goods to, the Partnership".

Findings

53. **This Review finds the Bank to be in compliance in regard to this item of the Complaint. Under EBRD Environmental Policy 2003 guidelines, it is not the task of this Review to adjudicate in an individual contract dispute at the level of the Portfolio Company.**
54. **EBRD guidelines and procedures regarding discriminatory practices that were in force at the time of the original investment in the Client are reflected in the policy statement adopted by AHK. There is also sufficient external legal recourse for an**

²³ Management Agreement between AHK and the Complainant dated 15 January 2012.

²⁴ Environmental Policy 2003, para 18

²⁵ Interviews with Environmental and Sustainability staff, 26th March 2018

²⁶ Ibid. para. 18 (iii)

²⁷ Amended and Restated Agreement of Limited Partnership, 30th March 2006, paras 4.1 (b) and (c).

aggrieved individual to pursue a claim of discrimination in hiring or firing, but the Complainant has not raised a legal case of discrimination under that legislation.

Complaint (b), (c), (d), (e) and (f)

55. b. That the removal of the Complainant from office was accompanied by the removal of other key employees of Kosovar nationality from their positions at AHK, thereby causing disruption and harm to them, to the operation of the company and to its reputation in Kosovo;
c. That the EBRD failed to promote decent work in its investment in the American Hospital;
d. That the EBRD failed to ensure implementation of national and international labour law and best practice by the Client;
e. That the EBRD failed to ensure that its contractor follows appropriate social standards;
f. That the EBRD failed to ensure that its client meets all applicable Performance Requirements.

These complaints are taken together for the purposes of this review, as they all relate to the manner in which due diligence was performed by the EBRD. A comprehensive overview of contingent procedures within the due diligence process is required to form a reasoned opinion on these matters.

The above elements of the Complaint are referenced by the Complainant to quoted text from the Environmental and Social Policy of 2008. It has already been established above that the relevant Policy for consideration under this review is the Environmental Policy 2003 that was in place at the time of signature of the Partnership Agreement²⁸. Nonetheless, the latter-mentioned policy as well as the Bank's 'Environmental Procedures for Private Equity Funds' give sufficient scope within which the concerns expressed may be considered.

Complainant's Position

56. In addition to the specific case concerning the manner of his personal contract termination, the Complainant claims that the Company:
- “• Installed fear and insecurity among Kosovar staff
 - Ruined the enormous efforts made in raising the human resources capacity of Kosovars in the health care sector.
 - Violated the objective of the investment by not working on sustainability of the project and allowing business practices that would prioritize financial interests only”²⁹
57. The Complainant further motivates these concerns by indicating that he wishes “to defend the main interest of the public interest of investment in this project, which is to build sustainable local Kosovar capacity to provide quality health care services in Kosovo.”
58. The Complainant adds: “...my concerns extend beyond my personal grievance and are focused also on local staff mistreatment, discrimination, unethical practices, violation of human and worker rights, fear, prioritization of financial interests versus capacity building and creation of opportunities for better treatment of population.”

²⁸ see above para. 39.

²⁹ Complaint No. 2017/05, See Annex.

59. The Complainant claims that the Company “Discriminated Kosovar professionals by not offering them publicly a chance to apply for managerial positions at the hospital”.
60. A letter of protest to the Chairman of the Board of AHK, signed by some 22 ‘physicians of AHK’ was given as supporting evidence of the widespread concern among core staff at this course of action. The letter states, inter alia: *“Very often, colleagues from Albania have behaved with disrespect for other colleagues, as a result only during the last 12 months we have lost more than 30 experienced colleagues, who have resigned or have been dismissed.”* It further points out *“the entire management team of the AHK will exist of Albanian citizens”* following the management changes referred to above.
61. An exchange of letters concerning the allegedly forced resignation of the Assistant Finance Officer of AHK were submitted as evidence of the extensive impact of the change in management style within the company at that time.
62. An important element of the Complaint is the allegation that there had been several cases in which former AHK employees had been subject to harassment and victimisation. The Complainant offered the contacts of eleven former AHK employees who were alleged to have suffered from such victimization. In the view of the Reviewer, sufficient detail was provided to validate their status as former employees of the AHK, but this cannot be verified by the Client because of the concern of those complaining to maintain confidentiality that is protected under EBRD procedures.³⁰ Brief questionnaires were sent to these eleven individuals and statements were received from 8 of them. All alleged a marked deterioration in industrial relations following the change of management leadership in 2015-16 that eventually led to their terminating employment with AHK. Some of those responding provided evidence showing that they had raised legal complaints regarding alleged unjust dismissal, but only one of these was so far pursued, others citing cost, delay and disillusion with the legal remedy as reasons for not persisting in their claims.
63. For the purposes of this Review it is not important whether these allegations were correct or not. There is no intention in this Review to audit the Company or to make findings with regard to its compliance. The focus of this Review, as has already been stated, is to understand whether the compliance mechanism used by the EBRD for this project was sufficiently robust to have identified relevant social issues (in this case, alleged discrimination) had they in fact existed.
64. The Complainant claimed that the American Hospital Board had not given sufficient opportunity for the full development of local Kosovar talent within the AHK before centralising control through the imposition of the Albanian management team. In his recollection the Board had claimed that it “had no time” to build local capacity as it desired structural control from the centre³¹.

Client’s Response

65. The Client strongly rejects these allegations. Stating: “SEEF II is proud of the achievements of the Company in establishing a leading presence in Kosovo...”, the Client continues:
“3. The success of American Hospital in Kosovo has created positive effects on multiple levels across Kosovo’s economy:

³⁰ Client comment to Draft Review of 12th July 2018

³¹ Interview by conference call with Complainant 16 April 2018.

- a. It contributed to retention of scarce qualified medical personnel in Kosovo, who decided to remain and work in Kosovo rather than emigrate in Western Europe after completing their studies
 - b. It provided a modern medical environment and a medium for continuous improvement of professional skills of medical personnel by addressing increasingly complicated pathologies and surgeries
 - c. It had a positive effect on taxes paid locally, as Kosovar patients were increasingly treated in the country rather than going abroad
 - 4. By way of example, with the exception of a limited number of physicians from Greece, Turkey and Albania who work in the Subsidiary, over 97% of the personnel and management positions are filled with Kosovar employees. This figure starkly contradicts the representation that Kosovar employees are not provided with opportunities to ascend to medical and management positions at the Subsidiary.
 - 5. SEEF II, on behalf of the Company and the Subsidiary, rejects allegations in relation to human and workers' rights violations by the Company or the Subsidiary.
 - 6. SEEF II, on behalf of the Company and the Subsidiary, rejects allegations made by the Executive such as (i) failure to promote decent work conditions, (ii) failure to implement national and international labor law and best practices, (iii) failure to ensure its contractors followed appropriate social standards, (iv) failure to ensure meeting of applicable performance requirements, etc. No evidence was provided to substantiate these claims because such claims are wholly without merit."³²
66. The Company claims that the letter of protest apparently signed by 22 'physicians of AHK' is a forgery. According to the Company, signatures gathered for another purpose were fraudulently appended to a new text by the Complainant.
67. The Company's Work Regulations covering Harassment and Discrimination were submitted as evidence by the Client³³. They seek to guarantee "*a working environment without discrimination*" and place a responsibility on local management to effect that guarantee.
68. Policies of the EBRD and OPIC were not only well known by the Client, but were also "the way we do business". As an impact investor, it was important to the Company to encourage best practice management as a means to build management capacity at local level³⁴. The internal work regulations of AHK contain clear policy against discrimination and on respect in the workplace. Section 1.6 of the AHK Work Regulations, in force since 2012³⁵, state "*All employees shall be treated and shall treat others with respect and dignity. Every individual is entitled to work in a professional environment, by promoting equal opportunities regardless of age, race, gender, religion, sexual orientation or disability. Employees shall not discriminate any individual or group of individuals or misuse the authority given to them. AHK shall not discriminate any individual in the selection, employment, appointment and performance of tasks and obligations of staff on the grounds of age, gender, race, religion, ethnicity or sexual orientation.*"
69. The Company pointed out that it had been a 'temporary' business decision to bring in a known and experienced management team to drive forward the expansion of AHK rather than to recruit from outside the Company and that currently some 97 per cent of the 354³⁶ employees of AHK are Kosovar. Allegations of pro-Albanian

³² Statement of Southeast Europe Equity Fund II, dated 5th October 2017

³³ Internal Work Regulation of AHK, Section 6, *Harassment and Discrimination*

³⁴ Interview of 16th April 2018

³⁵ AHK Internal Work Regulations 2012, Section 1.6 *Work environment and professional conduct*

³⁶ Client information to Draft Review of 12th July 2018

discrimination in appointments are therefore demonstrably unfounded³⁷. In this case the decision had clearly been a correct one, since the company now has over 75 per cent of the private health care market in the region. Its position in the market also demonstrated that there was no negative reputational impact on the company in Kosovo³⁸.

70. The Client pointed out that the Complainant had also put on notice the Inspectorate of Labour Rights under the Ministry of Kosovo, which conducted an audit during the respective period and found no evidence of unfair treatment in the Company³⁹.

The Bank's Response

71. The OPIC Consent Notice in respect of the proposed investment by the Fund in the Portfolio Company sets out the requirements for respect of worker rights and for compliance with the host country law and regulations.⁴⁰
72. OPIC conducted a pre-investment screening⁴¹ that was shared with EBRD and that showed no issues for concern.
73. As indicated above, Staff confirmed that the Bank does not actively monitor Portfolio Investments on the ground, because procedures do not require this and because a lack of resources would make it impractical to do so⁴². The focus of the Bank's compliance monitoring is the Client and the mechanisms that the Client has put in place to monitor portfolio companies.
74. As required by the Partnership Agreement, EBRD has received an Annual Environmental Report from the Client for each year of its operation.
75. The EBRD representative to the Advisory Committee of the Fund during the period of the alleged problems stated that there had not been any discussion of social compliance issues at meetings with the Client management and there is no regular item on the agenda that required a report on this topic⁴³.
76. Following receipt of the Complaint, a desk review had been conducted by staff of the Environment and Sustainability Department.⁴⁴

Observations

77. The EBRD is directed by its Establishing Agreement⁴⁵ "to promote in the full range of its activities environmentally sound and sustainable development".
78. As indicated above, the term 'environmental' is interpreted by EBRD's Environmental Policy 2003 in its wider meaning to include "*not only ecological*

³⁷ Statement of 5th October 2017

³⁸ *ibid.*

³⁹ Client comment to Draft Review of 12th July 2018

⁴⁰ OPIC Consent Notice, Southeast Europe Equity Fund II(B), L.P., 21st April 2008

⁴¹ OPIC 168A: Expedited Screening Questionnaire (ESQ) – Downstream Investments, Southeast Europe Equity Fund II (B), L.P., dated 3rd April 2008

⁴² Interview with EBRD Staff of 26th March 2018

⁴³ Information from EBRD Staff internal enquiry by telephone, 26th April 2018

⁴⁴ *Ibid.*

⁴⁵ Agreement Establishing the European Bank for Reconstruction and Development, 1990, Article 2.1vii

aspects but also worker protection issues, and community issues, such as cultural property, involuntary resettlement and impacts on indigenous peoples.⁴⁶

79. The Policy continues: “4. The EBRD will seek to ensure through its environmental appraisal process that the projects it finances are environmentally sound, designed to operate in compliance with applicable regulatory requirements, and that their environmental performance is also monitored. It will pay particular attention to requiring appropriate and efficient mitigation measures and management of environmental issues, which may have legal, financial and reputational implications, as well as environmental implications. It will seek to realise additional environmental benefits through the projects it finances, in particular if the projects also provide economic benefits..”⁴⁷
80. Paragraph 8 of the EBRD’s Environmental Policy indicates:
“8. The EBRD will actively seek, through Bank financed projects, to contribute to the implementation of relevant principles and rules of international environmental law. These principles and rules are set forth in instruments such as treaties, conventions and multilateral, regional or bilateral agreements, as well as in relevant nonbinding instruments.”
81. Thus, it is clear that the issues raised by the Complainant are within the scope of the EBRD’s environmental requirements for operation of the Fund.
82. As due diligence for this project was operated via the OPIC Procedures, a screening study was undertaken by OPIC in April 2008, prior to the Fund’s investment in the AHK (at that time called UniversAlb) and results shared with the EBRD. The screening study consists of a self-completed questionnaire from the Client that indicates the following issues relevant to the present Complaint:
- 100 per cent of Management and 40 per cent of Professional/Technical staffs would receive formal training. Some of that training would involve external training in Turkey and Western Europe;
- The Company did not at that stage have a written equal employment policy that adhered to the ILO Convention 111, but the Client undertook that it would adopt such a policy;
- The Client expected AHK to provide health coverage and daily meals to its employees.⁴⁸
83. The Annual Environmental Reports of the Client give only very brief summary information on each Portfolio Company and, in the case of AHK, the entry in every reporting year has been confined to the single sentence: “*The company has no operations that are known to have adverse environmental impacts*”⁴⁹. This falls short of the requirements of the EBRD’s own ‘Environmental Procedures for Private Equity Funds’ that require, inter alia:
(i) a summary of the main health, safety and environmental issues identified in the environmental due diligence and how they have been addressed (see para 90 above for a number of socially relevant environmental issues);
(ii) a note of any complaints against the company; and
(iii) a description of how the borrower’s environmental performance has been monitored.

⁴⁶ EBRD Environmental Policy, 2003, para 3.

⁴⁷ Ibid. para. 4

⁴⁸ Ibid.

⁴⁹ SEEF II (B) Environmental Reports, 2005 through 2015, BCM to EBRD.

84. No mention is made in any of the Annual Environmental Reports from the Client of the existence of complaints against the Company, including that by the Complainant and legal challenges that were brought by at least two of its former employees.
85. Statements from 8 former employees and a petition signed by 22 of the Company's physicians protesting the changes in management suggest that there was concern at the level of AHK staff in the midst of considerable organizational change, rightly or wrongly. Active protest by approximately 8.5 per cent of the total Company staff shows some evidence that a 'climate of fear' as alleged may have existed among some AHK employees around that time. If the protest letter from the 22 physicians of AHK was a forgery, as the Company suggests, this was an even more serious situation that was surely one that the Company would have discussed internally at the very least. Yet no discussion or explanation of the protest letter was ever discussed by the AH Advisory Board. The issues raised in the protest letter are not a subject for investigation by this Compliance Review under the 2003 Environmental Policy but the existence of such a letter is relevant in view of the comment by the EBRD member of the Fund's Advisory Board that no social issues were ever discussed at review meetings. It seems quite extraordinary that an allegedly forged attack against the social policies deployed by the Company and orchestrated by its former Executive Director should not have found its way to the attention of the compliance oversight mechanism. A robust compliance mechanism would require regular review at board level of its own internal compliance and of any challenges being raised to it. The Client was able to confirm that no such item was ever placed upon on the Board's agenda⁵⁰.
86. An EBRD FI Sustainability Index Report⁵¹ was conducted by an external service provider with the Client for the year 2014 in respect to its investment in American Hospital. This took the form of a self-assessment questionnaire. Responses to the question "*What level of concern does your institution have in relation to the following sustainability issues?*" Evoked the responses:
 - "Worker/Management relationship – Slightly concerned
 - Community impact – Slightly concerned
 - Human rights – Very concerned"

There is no evidence that these responses were followed up within the Bank's monitoring procedure.
87. The Company claims that its policies are to uphold the local law and to operate according to best practice guidelines and that it has incorporated the Investment Guidelines of the Fund into its basic management philosophy – its "way of doing business"⁵². The Client points out that independent audits and reviews by various institutions in Kosovo dealing with labour rights and labour protection support this claim⁵³.
88. Kosovo has a world-class and up-to-date 'Anti-Discrimination Law'⁵⁴. No claim has been made by the Client or other former employees of AHK under this law.
89. The internal regulations of the AHK in force since 2012 contain strong written policy against discrimination of any kind.⁵⁵ Those regulations do not, however,

⁵⁰ Client response to Draft Review of 12th July 2018

⁵¹ EBRD FI Sustainability Index Report, Price Waterhouse Cooper, 2014

⁵² Interview by conference call of 25th April 2018

⁵³ Client response to Draft Review of 12th July 2018

⁵⁴ 'The Anti-Discrimination Law', Law no. 2004/3, adopted 19th February 2004.

contain a robust mechanism for the confidential reporting and investigation of specific instances of harassment or discrimination, instead relying simply upon a single-step procedure. The procedure requires only that any complaint should be addressed to the supervisor who will decide on action together with the HR Department. This is clearly inadequate to deal with cases where the matter in dispute concerns alleged discrimination by a member of the management team.

90. Respondents to the confidential questionnaire who claimed to have suffered harassment at AHK and who had used the grievance mechanism claimed either to have received no response or to have suffered a further worsening of their situation as a result of their complaining.
91. As indicated above (para 20), it is not the task of this Review to comment upon actions or inactions of the Client and nothing in this Review should be interpreted as a finding against any action or inaction by the Client in this regard. The task is rather to review whether procedures adopted by the Bank for monitoring the activities of its Client would have been sufficient to have identified such environmental and social problems had they occurred. In this case, it is not necessary to establish whether or not any specific claims are accurate in their detail, or whether the Company did or did not practice discrimination, but to establish that the procedures adopted by the EBRD for monitoring this investment were sufficient to ensure that issues of discrimination could not have escaped detection were they to have arisen in the context complained of.
92. Kosovo's proclamation of independence from Serbia in February 2008 and the tensions surrounding that event revived public and political discussion about a 'Greater Albania' across the Balkan region⁵⁶. There is a substantial minority voice in Kosovo for eventual unification with Albania that is expressed by the main opposition party, *Vetvendosja*. This view has not been shared so far by the majority of Kosovars on the evidence of election results. Many who do not support the notion of eventual unification point to the different political and social history of the two populations during the period when Albania was within the confines of the Soviet Union's centralised economy, while Kosovo was a part of the self-managing socialist economy of the former Yugoslavia. The cultural and social impacts of this history and distrust of Albanian domination were indicated as components of the problem by the Complainant in interview⁵⁷ and in some responses to the confidential questionnaire. The sensitivity of local employees to these matters may have played a role in their response to a temporary transfer of management authority in the Company.
93. There are no specific requirements or procedures under the 2003 Environmental Policy indicating what is considered best practice for hiring and firing. Had the current Environmental and Social Performance Requirements of the Bank been in force for the Client, a greater level of transparency and accountability could have been expected at the level of the AH Advisory Board in regard to the appointment of a whole new Board of management at AHK. The resulting gap in expectations resulting from a fast-developing social awareness and expectation of transparency and equal opportunities versus a static interpretation of requirements deriving from procedures designed more than a decade earlier are a factor in this case.

⁵⁵ AHK Work Regulations 2012, section 1.6, Work environment and professional conduct and Section 6. Harassment and Discrimination

⁵⁶ See, for example, 'Albanian-Kosovo relation: Quo Vadis?', Ilir Kalemaj, Friedrich Ebert Stiftung, 2014

⁵⁷ Interview by conference call of 16th April 2018.

Findings

94. This Review finds that the Bank failed to comply fully with its responsibilities to monitor the effectiveness of the Client's environmental performance as required by the EBRD Policies and Environmental Procedures for Private Equity Funds, Annex 8, and Annual Environmental Report.
95. This Review also finds that the practical application of the 2003 Policies and Procedures lacks the pro-active "promotion of environmentally and socially sustainable development" that is foreseen in the Bank's Establishing Agreement⁵⁸. Compliance was outsourced to OPIC and relied on self-assessment and monitoring by exception that would have been insufficient to give early warning of issues that might raise concern but which the Client was not attuned to reflect. The Bank's representation on the Client's Advisory Committee was not able to pick up on these issues.
96. The Review also notes that the Bank has considerably developed and expanded its policies and guidelines governing in particular its requirements for oversight of management systems and procedures within client FIs since its original investment in the Fund. It has also developed its performance requirements for Labour and Working Conditions since that time.
97. In regard to these latter points, the Review therefore suggests Recommendations to improve the Banks' effectiveness in monitoring historical ongoing FI projects in future.

Recommendations

98. This Compliance Review has been conducted within the terms of the EBRD's Environmental Policy 2003 and associated procedures in line with the Bank's ToR. EBRD's current Performance Requirements, however, deal much more comprehensively with the management environmental and social systems performance, requiring *"a methodical systems approach comprising planning, implementing, reviewing and reacting to outcomes in a structured way with the aim of achieving a continuous improvement in performance management"*. This perspective is now publicly promoted by the Bank as an integral part of its current operation and vision. The Bank's publics could be expected to understand from this that the avowed principles apply across the Bank's portfolios.
99. The management of environmental and social performance as a 'dynamic' process of 'constant improvement' is not reflected in an exemption from current recognised management standards for projects funded before 2008. This anomaly allows projects that have been started up over a decade previously to continue to operate according to compliance criteria that are out of date with the Bank's own current vision of its responsibilities – even for sub-investments that have been entered into after that date. For the Bank's operating staff this is a confusing situation likely to lead to the misapplication of policy.
100. It is strongly recommended that the Bank address this inconsistency in its own Procedures and Performance Requirements in order to ensure that all projects are brought within a commonly understood and administered framework of compliance.

⁵⁸ Ibid.

101. This will require that investment agreements with clients contain language that foresees the need to update compliance requirements in line with changes introduced in the pursuit of “continuous improvement of performance management”.

Conclusion

102. This Review considers that the procedures put in place by the Bank to monitor compliance of the Client did not fully meet the requirements of its Environmental Procedures for Private Equity Funds that were the policies and procedures agreed for governance of the Fund at the time of initial investment in 2005. However, those procedures are also deemed inadequate to give risk assurance that the Fund and its sub-projects continue to meet present-day requirements as publicly promoted by the Bank more than a decade later and that call for a dynamic process of continuous improvement of performance management. Recommendations are offered for bringing the Bank’s full active portfolio within a commonly understood and administered framework of compliance.