

Environmental and Social Review Summary (ESRS) Mercon – Regional

Original language of the document: English
Revision's cut-off date: February 2021

1. General Information of the Project and Overview of Scope of IDB Invest's Review

This Project aims at supporting Mercon Coffee Group (“Mercon” or the “Company”) activities across the coffee value chain from production and storage in countries of origin like Guatemala, Honduras, and Brazil (countries of the Project) to transportation and commercialization in multiple destinations. This Project prioritizes improving farmers’ access to markets and finance, provision of technical expertise, and climate-smart considerations.

In 2017 and 2018 the Dutch Entrepreneurial Development Bank (FMO) provided three long-term loans to support Mercon operations in Nicaragua. In 2019 the International Finance Corporation (IFC) proposed a revolving credit facility in favor of Mercon to support its activities across the coffee value chain in Guatemala, Honduras, Nicaragua, Brazil, and Vietnam. The Environmental and Social Review Summary (ESRS) prepared by IFC, including implementation progress status and Environmental, Health and Safety (EHS) road map and Correction Action Plan 2019-2021 from their lender meeting in March 2019, was shared with IDB Invest.

The environmental and social due diligence (ESDD) process included the review of supporting information such as: EHS policies, plans, manuals, and procedures; human resources policies; occupational health and safety (OHS) programs; waste management information (both hazardous and non-hazardous waste, or waste requiring special handling); procedures for monitoring and evaluating environmental conditions at work (e.g., air, noise, and effluent emissions); and emergency response plans, among others. This process was complemented by a site visit to Nicaragua in February 2020, to the San Carlos dry mill facility in Matagalpa and coffee growing areas and LIFT Program. It also included meetings with Mercon’s Chief Executive Officer, Chief Finance Officer, Finance Director, Origin Director for Latin America, Sustainability Director, Project Manager for Central America, EHS coordinator, LIFT Coordinator, and Human Resources Director.

2. Environmental and Social Categorization and Rationale

The Project has been classified as a Category B operation according with BID Invest’s Environmental and Social Sustainability Policy since overall, its environmental and social risks are expected to be reversible and capable of being mitigated through currently available technologies.

Given the Project's characteristics (in terms of the use of financial resources), in which the acquisition of new land is not foreseen, but rather a productivity increase on already owned land and through third parties suppliers, the possible environmental and social impacts and risks during operation and maintenance (“O&M”) of the Project will be: (i) the production of hazardous and non-hazardous waste; (ii) polluting atmospheric emissions (mainly dust from field preparation, the transit of vehicles and agricultural machinery, and combustion gases from vehicles and agricultural machinery); (iii) generation

of industrial and domestic wastewater; (iv) occupational health and safety risks for workers; and (v) use of resources, such as energy and water sources (surface or underground), mainly.

The Project triggers the following IFC Performance Standards (“PS”): i) PS1: Assessment and Management of Environmental and Social Risks and Impacts; ii) PS2: Labor and Working Conditions; iii) PS3: Resource Efficiency and Pollution Prevention; iv) PS4: Community Health, Safety, and Security; and v) PS6: Biodiversity Conservation and Sustainable Management of Living Natural Resources.

3. Environmental and Social Context

3.1 General characteristics of the Project’s site

Mercon is a vertically integrated coffee company. Its footprint encompasses all segments of coffee value chains, from (i) upstream Robusta production on 684 ha, as of May 2019, distributed in three farms on the Atlantic side of Nicaragua (La Esperancita with 92 ha, San Antonio with 379 ha and San Jose with 213 ha), with a total land cover of 1,545 ha, including forest conservation area; (ii) midstream operations, including 14 wet and dry mills - four under its own management within the Projects countries (Nicaragua/San Carlos; Nicaragua/La Luz; Nicaragua/El Carmen; and Honduras/CIGRAH) and eight third-party mills (Brazil/ Acaua Armazens Gerais Eireli; Brazil/ Alameda do Café; Brazil/ Cafeco Armazens Gerais LTD; Brazil/ Dinamo Inter Agricola; Guatemala/ SUBE, S.A.; Guatemala/ Santa Rita; Guatemala/Santa Isabel; Guatemala/RCMA) located in countries of origins to maximize value-addition and job creation and 109 warehouses (e.g. buying/collection centers); and, (iii) downstream coffee sourcing and trading operations in nine countries (Nicaragua, Honduras, Guatemala, Brazil, Vietnam, Panama, USA (Miami) and Europe (Spain/Netherlands).

Mercon sources raw green coffee beans from more than 9,000 third-party suppliers and distributed its Arabica and Robusta coffee in 40 countries to end-customers (e.g., illy, Lavazza, Caffe Nero, Paulig, Starbucks, Kraft Foods, Nestle North America). In all origins, Mercon strategy is mainly focused on small producers but not only. An estimated 80% of its coffee suppliers are sourced from small farms (of less than 12 ha), 15% are medium-sized farms (between 12-25 ha), and 5% are large farms (more than 25 ha), as follow: (i) In Guatemala, the sourcing is 60% from small producers and 40% from intermediaries; (ii) In Honduras, the sourcing is from intermediaries (small/medium) but it intends to increase its direct relationships with small producers; (iii) In Nicaragua, the sourcing is from 5,000 small producers (no intermediaries involved) at country-wide level; and (iv) In Brazil, the sourcing is from large cooperatives and producers, but is based on spot purchasing in all producing coffee regions.

To comply with coffee requiring higher sustainability assurance, especially for the Robusta species, Mercon meets voluntary Agro-commodity Standards such as: Rainforest Alliance – RFA and UTZ¹, Nespresso AAA Sustainability Program², among others.

¹ By January 2018, UTZ merged with Rainforest Alliance. UTZ certification shows consumers that products have been sourced, from farm to shop shelf, in a sustainable manner (to learn more, go to: <https://utz.org/what-we-offer/certification/>).

² In 2003, Nespresso together with Rainforest Alliance initiated the Nespresso AAA Sustainable Quality™ Program <https://www.nespresso.com/de/en/thepositivecup/initiatives/aaa-sustainable>.

Leading Innovation and Farmers Traceability (LIFT) Program

Mercon has been rolling-out an internal agronomic program entitled “Leading Innovation and Farmers Traceability” (LIFT) since 2015. The main objective of the LIFT program is to manage the “first mile” of Mercon’s supply chain, thus providing coffee traceability to the farm level. This program dedicated to smallholder producers has three main pillars, (i) to increase of coffee productivity by 40% within three years, (ii) to promote environmental management (reforestation, conservation of water resources, protection of natural forests and soil improvements); (iii) to promote social development (education).

LIFT provides short-term, pre-harvest and harvest financing, and long-term financing for farm rehabilitation, planting material, effluents management, technical support to achieve voluntary certifications (e.g. Rainforest Alliance – RAF and UTZ). The LIFT program is being implemented by a team of 32 agronomists, each supporting/having oversight of 80-100 Arabica producing farmers, and 3 agronomists for the Robusta sourcing (estimated at 300-400 suppliers on 2,500 ha). All Robusta suppliers have been included into the Nicaragua’s LIFT program.

Overall, in 2019, 31% of total coffee volume sourced in Nicaragua are from LIFT producers (traceable/certified), 5% of total coffee volume in Honduras are from LIFT producers (traceable/certified), and 7.58% from LIFT producers (traceable/certified) in Guatemala. The Company is aiming to have 70% of total sourcing from Nicaragua under its LIFT program. These strategies are under development for all other origins.

4. Environmental Risks and Impacts and Proposed Mitigation and Compensation Measures

4.1 Assessment and Management of Environmental and Social Risks

4.1.a E&S Assessment and Management System

Mercon’s EHS Management System is in its development phase for all class of assets (farms, mills, warehouses, and sourcing operations). Since 2017, it started establishing gradually the building blocks of an integrated EHS management system for its operations, including (i) securing senior management commitment to be a sustainability leader in coffee production in Nicaragua, (ii) achieving 100% sustainable/certified sourcing from pre-financed suppliers, including rolling out the LIFT program in all origins, (iii) adopting a Corporate Responsibility and Sustainability (CRS) policy, (iv) establishing a Board’s CRS Sub-Committee, (v) developing and effectively implementing an OHS management system at its Nicaraguan mills, including a Master List of EHS Standard Operating Procedures (SOPs), Working Instructions and establishment of safe work permit system (e.g. confined space, hot work, working at height, Lockout-Tagout - LOTO), and (vi) disclosing an annual Sustainability report.

However, to achieve compliance with international EHS Management Systems standards, Mercon shall include: (i) implement the Farm and Supplier Codes applicable to its farming and sourcing operations; (ii) further implementation of comprehensive multi-year environmental and OHS audits and management plans to all operations (farms, mills, warehouses and sourcing) addressing risks and impacts (e.g. water supply, including hydrogeological study and sustainable extraction yield, wastewater treatment, ambient and point source air emission, solid and hazardous waste management, safe hazardous material storage) based on internal/external EHS audits, with the preparation of Corrective Action Plans (CAPs), as necessary; (iii) monitoring and reporting of environmental management plans, including Key Performance

Indicators (KPIs) allowing Mercon to assess its overall environmental compliance and performance; (iv) finalize and implement the supply chain risk assessment and management procedures of its sourcing operations; and (v) develop and implement EHS/labor requirements applicable to contractors, including due diligence, monitoring oversight, and enforcement.

As part of the development of the EHS Management System, Mercon is in the process of further consolidating a legal and regulatory registry for all applicable EHS requirements to its operations. Therefore, to fully comply with PS-1, the Company will evaluate the integrity of the EHS Management System in accordance with the IFC implementation Manual and Tools³. The results of this evaluation will allow strengthening or updating the components of the corresponding EHS Management System according to the applicable environmental, social, health, and safety requirements set forth in the environmental and labor legislation of the countries of the Project.

4.1.b Policy

In 2018, Mercon' Board of Directors formally adopted a Corporate Responsibility and Sustainability (CRS) Policy. However, relevant to its sustainability framework, in 2020 Mercon developed three group-level policies: (i) Environmental; (ii) OHS; and (iii) Stakeholder Engagement.

Also, during 2020 and early 2021, the Company defined a Farm Code, applicable for its Robusta farms in Nicaragua, and a Supplier Code, applicable to its sourcing operations in all origins. However, Mercon had already implemented the provisions defined in the Farm Code, using RAF, UTZ and Nespresso AAA sustainability requirements as technical and E&S specifications for the establishment of its three Robusta farms in Nueva Guinea, Nicaragua.

4.1.c Identification of Risks and Impacts

4.1.c.i Direct and indirect impacts and risks

As a result of establishing and implementing a process for identifying and assessing EHS risks and impacts for its upstream (farms), midstream (mills and warehouses) and downstream (sourcing) operations, Mercon started in 2018 the implementation of an environmental audit program at its two mills in Nicaragua (San Carlos and La Luz). This program will be extended to its Nicaragua (El Carmen) and Honduras (CIGRAH) mills and the 8 rented mills in Guatemala and Brazil and the result of these audits will be summarized into a Corrective Action Plan (CAP) with assigned budget defining the environmental management plans to be implemented at each facility.

As it relates to OHS risk assessment, mills' workplace risk assessment has been completed and recommended mitigation measures (e.g., procedures, work permit, PPEs, training) have been successfully implemented at Nicaragua San Carlos and La Luz mills, and at the rented mills in Guatemala (Sube and Santa Rita).

For its sourcing operations, Mercon is dedicated to achieving 100% traceability of all direct (pre-financed) third-party suppliers through mobile devices application, which provide GPS coordinates and completion

³ Environmental and Social Management System, Implementation Manual - General, IFC, version 2.1, November 2015. Environmental and Social Management System Tools – General, IFC, version 1.2, November 2015.

of E&S indicators/questionnaire. This has been successfully completed in Guatemala, Honduras, and Nicaragua.

4.1.c.ii Gender risks

Woman's gender-based violent death is the most serious expression of violence and is usually the culmination of continuum of violence and discrimination that women face in their lifetime. In this context, according to the Central American Integration System⁴ (SICA), the countries of the Project, note a femicide rate (Guatemala, 2.5; Honduras, 10.2; and Nicaragua, 1.5) significant higher than the rest of Central America (average of 0.7, excluding El Salvador⁵).

Based on the above, the Company shall develop a base line study on equity, diversity, and inclusion, which includes gender and gender-based violence (GBV) risk, in all the countries of the Project and based on the findings elaborate a CAP to attend the critical issues. Meanwhile, internally the Company is addressing these gender related aspects within their policies and procedures (refer to PS-2, Human resources policies and procedures).

4.1.c.iii Climate change exposure

Precipitation patterns in Latin America are shifting, temperatures are rising, and some areas are experiencing changes in the frequency and severity of weather extremes such as heavy rains and droughts.

Therefore, Mercon shall develop a climate change exposure risk assessment study for its farms and supply chains in all the origins and will provide a crop adaptation to climate change program for each coffee variety (Robusta and Arabica).

4.1.d Management Programs

In Nicaragua, Mercon's milling operations are still in the process of fulfilling the Terms and Conditions of the Environmental Licenses issued by the Ministry of Environment and Natural Resources (MARENA, for its acronym in Spanish). Two of the three coffee mills in Nicaragua, San Carlos and La Luz, have developed and implement an Environmental Management Programs (EMS) to comply with the environmental law and achieve their environmental license. On the other hand, El Carmen EMS has been submitted to MARENA for final review and approval and is still pending its environmental license. In Honduras, CIGRAH mill received its environmental license in 2002 from the Ministry of Environment in that country.

According to the above, Mercon shall develop a compliance matrix of all legal and contractual obligations of each existing operating facility, including: (i) the competent authority that grants the authorization or issues the permit or license; and (ii) the issue and validity dates.

⁴ "Resolution Relating to the Updating of the Regional Policy on Equity and Gender Equality of the Central American Integration System (PRIEG/SICA)"; Council of Ministers of Women of Central America and the Dominican Republic (COMMCA) XLII Regular Meeting on February 7, 2018.

⁵ El Salvador is considered one of the most violent countries in Latin America, a situation that also affects women, girls, and adolescents in a differentiated manner.

Also, the Company shall develop and implement a Procedure for Corporate Environmental Management Monitoring Visits intended to define the guidelines, responsibilities, and methodology to identify, access, update, communicate, evaluate, and follow up on compliance with legal requirements related to its business activity, as well as to identify opportunities for improvement in the environmental performance of each operating facility. Also, shall design a training program on the use of this procedure, for its implementation and disclosure to all its personnel.

4.1.e Organizational Capacity and Competency

Mercon has established an organizational structure to ensure the development and effective implementation of its sustainability strategy, namely a Board's CRS sub-committee. This sub-committee has the responsibility to analyze the sustainability/EHS risks and opportunities potentially impacting Mercon's business strategy. The coordination of this committee is under the responsibility of the Sustainability Director, who also defines the annual sustainability programs and tools for their implementation in all countries/operations. Mercon's wet/dry mills and warehouses have assigned plant-level EHS coordinator, OHS supervisors and Human Resource (HR) officers who are responsible to ensure compliance with EHS/labor legal and regulatory requirements. In compliance with national labor regulatory requirements, plant-level OHS Committee, composed of management and worker's representatives, and an Emergency Preparedness and Response Group have also been established at all operations.

Also, Mercon sourcing team is led by an Origin Director in Latin America and the LIFT coordinators which is composed of 35 agronomists, including 31 in Nicaragua, 2 in Honduras and 2 in Guatemala. Additional agronomists will be recruited in the next years as the LIFT is expanding in all origins.

4.1.f Emergency Preparedness and Response

Emergencies associated with coffee farming, milling and storage may include dust explosion, fire, chemical spills, structural or power failures, and natural disasters. Mercon has developed and implemented an Emergency Preparedness and Response Plan (EPRP) for the San Carlos and La Luz mills in Nicaragua, which includes the designation of an Emergency Committee and several brigades (evacuation, first aid, fire prevention and communication brigades). This plan identifies the areas where accidents and emergency situations may occur, the response procedures (for fire, earthquake, flood and hurricanes, civil unrest and theft), an inventory of the equipment and resources available and the designation of responsibilities. It is based on best safety standards, engineering design and risk management practices, and is reviewed annually.

In March 2016, the EPRP for the San Carlos mill was approved by the Matagalpa Fire Department, as compliant to the technical requirements on protection against fire. Periodical emergency preparedness training (annual) and fire drill (every semester) are provided to the personnel, including the participation of the Local Fire Department.

Mercon has confirmed that similar EPRP exists for all locations (mills and associated warehouses) in the countries of the Project.

4.1.g Monitoring and Review

To monitor the EHS performance of its farms, mills, and sourcing operations, Mercon started defining mandatory KPIs and reporting them on its three-year EHS workplan. In 2017, for its environmental monitoring, the Company established basic KPIs to monitor energy (electricity, diesel, petrol and LPG) and water consumption. However, to comply with PS-1, Mercon shall establish a comprehensive set of environmental KPIs to cover additional bio-physical parameters, such as: liquid effluents, solid and hazardous waste management, ambient and point source air pollution monitoring, noise, etc.; and performance targets, among others: estimate of Greenhouse Gas emissions and reduction targets.

Also, the Company shall develop internal annual EHS/Sustainability performance audits, carried out by Mercon's Sustainability Director, EHS coordinator and plant-level OHS Committees. The findings and recommendations will be submitted to the CRS Sub-Committee for review and amendments of the Sustainability Strategy will be performed, as needed.

Finally, Mercon undergoes regular independent audits from its coffee products off takers as part of the implementation of the Buyers' Supplier Code of Conduct. Recommended corrective actions have been successfully implemented based on supporting documentation for corrective/preventive non-conformities or are in the process of such, to maintain annual certification of third-party voluntary standards (e.g., RFA, UTZ).

4.1.h Stakeholder Engagement

As part of its materiality assessment of 2018, Mercon has identified and mapped its main stakeholders and has engaged into a consultation process. They also developed a Stakeholder Engagement Policy, which is under review by Mercon Group' CSR sub-committee.

Once this policy is approved, the Company shall implement a Stakeholder Engagement Plan (SEP) for each country of the Project, that includes the following: (i) updated identification of all stakeholders and affected communities (if any), who may be interested in the Project; (ii) differentiated measures to enable the effective participation of disadvantaged or vulnerable groups; (iii) mechanism to ensure that community representatives reflect the views of affected communities; (iv) details on how information is shared with stakeholders; (v) details on the participatory process among affected communities and how the grievance mechanism can be accessed.

The Company is pro-actively supporting multi-stakeholder's sustainability coffee roundtables which are aligned with its business model focusing on coffee farm renovation, climate resilient coffee production through agronomic practices and seed varieties, and traceable/certified sourcing. Partnership has been established with such roundtables and research institutions, such as Sustainable Coffee Challenge, International Organization for Coffee, World Coffee Research, Coffee Center at University of California in Davis.

4.1.i External Communication and Grievance Mechanisms

4.1.i.i External communication

Mercon started reporting, on an annual basis, on its E&S and OHS KPIs (Sustainability Report) to all its stakeholders using the format and indicators as prescribed by the Global Reporting Initiative⁶ (GRI). This activity continues and for upcoming reports, the Company will increase its coverage to all its origins.

4.1.i.ii Community grievance mechanism

Building on its Code of Conduct reporting mechanism and acknowledging that Mercon's operations have very limited potential risks and impacts on surrounding communities. However, the Company is in the process of defining a Community Grievance Procedure, allowing stakeholders to communicate their grievances about Mercon's environmental and social performance. This grievance mechanism will allow for anonymous complaints and complaints related to sexual harassment and/or to security forces. Also, the Company will establish a logbook to record such complaint and document resolution process and implement a Training Program on the use of this grievance mechanism, for its implementation and disclosure to all its personnel, including contractors and subcontractors, and other stakeholders.

4.1.j Ongoing Reporting to Affected Communities

As mentioned before, it is not foreseen to have potential risk or impacts on local communities directly affected by the Project. However, Mercon's annual Sustainability Reports and grievance mechanism are available for any community or stakeholder.

4.2 Labor and Working Conditions

4.2.a Working Conditions and Management of Worker Relationships

In February 2019, Mercon employed 650 direct (full-time) employees. In term of gender breakdown, there is 65% male and 35% female. More than 58% of the Companies permanent workers are within the range of 18-35 years old. During the crop season, additional workforce is hired as temporary staff, which by the 2018/19 on-peak season, reached 3,650 hires.

4.2.a.i Human Resources Policies and Procedures

Mercon's HR team have adopted a set of corporate values (integrity, excellence, teamwork and entrepreneurship) and a robust corporate Human Resource Management System in 2017 which provides a comprehensive range of policies and procedures under five main themes, namely (i) compensation and benefits (salary administration, temporary assignment, promotions, bonus); (ii) recruitment (permanent and temporary employees); (iii) training (assessment needs, onboarding); (iv) performance appraisal; and, (v) compliance (e.g. overtime, vacations, maternity leave).

The reference documents for the development of its Group-level HR Policies and country-level Manual of Procedures included the applicable Labor Code in all countries of origin, ILO Conventions, IFC PS 2, Fair

⁶ G-4 Guidelines.

Labor Association, sector-based requirements as well as GRI HR related monitoring/reporting indicators. These requirements apply to all workers (permanent and temporary) at all workplaces where Mercon maintains management control, including its farms, mills, warehouses, and offices.

In addition, by 2016 Mercon adopted a Code of Conduct which formalize its corporate commitment towards applying ethical standards to its employees and business partners, including contractual agreement with employees (permanent / temporary), conflict of interest, relationship with suppliers and service providers, professional security management practices, prohibition of sexual harassment and/or bullying, and process of disclosing whenever non-compliance with the Code occurred.

The Group-level HR policies and country-level procedures, together with the Code of Conduct are applicable to all permanent (indefinite term of contract) and temporary workers, including seasonal employees. Each new employee undergoes an induction session which include the reading and signing of his/her understanding of the HR framework and Code of Conduct. An Employee HR Handbook is given to all employees following the induction session.

However, to fully comply with Ps-2 and address the gender and GBV within the countries where Mercon operate, the Company will define a strategy to consider the gender related aspects, such as equal opportunities (“gender smart policies”), sexual harassment and bullying (“respectful workplaces”), and GBV within HR policies and procedures, Code of Conduct and Code of Ethics, including adapting their Community Grievance Mechanism to be able to capture and address grievances related to GBV and sexual harassment.

The HR function is led by a Human Resources Director and is composed of 24 staffs covering all countries/operations. The respective management team in all countries of operations has the primary responsibility to ensure that all the workplaces under their management authority adhere to Mercon HR policies and procedures, and the head of any workplace is responsible to ensure day-to-day implementation and operational control for the provisions described in the policy. Inspection by the country-level labor authority also takes place annually (e.g., in Nicaragua, by the Ministry of Labor).

4.2.a.ii Working Conditions and Terms of Employment

Mercon complies with the labor compliance framework of each country of operation for minimum wage, working schedule, overtime, holidays, probation period, labor contracts, for fixed (permanent employees) and determined (temporary workers). For salaries, Mercon complies with the minimum wage salary of the sector in each country of operation and perform salary benchmark within the coffee sector to guarantee external competitiveness. All permanent employees are subject to the salary review policy, that can be done every 2 years or yearly, depending on how the market information grows and the financial situation of the Company.

Additionally, the Company provides in certain countries, complementary benefits to the employees such as: health insurance, life insurance, transportation, employee discounts (dentists, ophthalmologist, exercises in the office instalments, among others). For temporary workers in the mill, Mercon provides free shuttle for employees working on night shifts and an attendance bonus for special holidays (Christmas and New Year’s Eve) and for those working in the fields, the company can offer accommodations under certain conditions and through a prior agreement.

For upcoming years, Mercon is analyzing whether it will continue to offer accommodations to the temporary workers in the fields. In this case, to fully comply with PS-2, the Company shall develop and implement a Workers' Accommodation Manual, for both the Company and subcontractors' facilities, that defines processes and standards applicable to: (i) appropriate construction standards; (ii) provision of adequate and sanitary living conditions; (iii) provision of appropriate leisure and health facilities; (iv) the type of staff to manage the facility; (v) appropriate management policies, such as security and grievance procedures; and (vi) ongoing liaison with local communities. This manual will be based on IFC/EBRD⁷ Guidance Note on Workers' Accommodation, adaptable with the local context of each country where the Company operates.

In this regard, Mercon shall implement an annual housing satisfaction survey for the inhabitants of the Workers Accommodations Facilities to obtain direct feedback from users/beneficiaries on the facilities most prominent aspects and the main areas of opportunity that could be addressed gradually through a specific CAP.

4.2.a.iii Workers' Organizations

Mercon has established policy and procedures which explicitly support the rights of freedom of association and workers seeking collective bargaining agreement. Even though Mercon does not forbid workers to organize themselves in a union or bargain collectively, such provision has not yet materialized in any of Mercon operations.

4.2.a.iv Non-discrimination and Equal Opportunity

Mercon is committed to establish a work environment based on the principles of equality, non-discrimination, and fair treatment in compliance with applicable labor code and its Code of Conduct. Such commitment is reflected in the Group-level HR Policy against any forms of discrimination in hiring, compensation, access to training, promotion, etc. based on race, origin, age, gender, etc.

4.2.a.v Grievance Mechanism

Mercon has establish a Worker's Complaint and Resolution Management Procedure which is managed internally ("my voice"). However, to fully comply with PS-2, the Company will update and improve its procedure to: (i) allow for anonymous complaints; (ii) allow complaints related to sexual harassment and GBV; (iii) ensure that all permanent, temporary, seasonal, and casual workers and contractors can access such mechanism; (iv) disclose and communicate it throughout the organization; and (v) establish a formal Mercon Group and plant level Grievance Committee.

The procedure will reflect, through a diagram, the steps to be taken by workers/contractors to manifest any concerns, including through anonymous channels, contact responsible persons, engage in mediation process, and provide timely feedback. It will also ensure that all permanent, temporary, seasonal, and casual workers and contractors can access such mechanism, and will be included into the country-level HR Manual of procedures and Employee Handbook.

⁷ European Bank for Reconstruction and Development (EBRD).

Awareness of this procedure will continuously take place during staff induction session. Farms, mills and sourcing managers and supervisors will be trained to ensure effective implementation. Training to Mercon permanent / seasonal workers of such procedure and access to logbooks will be scheduled afterwards. Finally, complainants may remain anonymous, and analysis of systemic issues will be documented and addressed.

4.2.b Protecting the Workforce

Mercon adopted a procedure for prohibiting use of child worker and forced labor in alignment with applicable country-level Labor Codes in all countries of operations. As stipulated in its HR Recruitment Policy, minimum age of employment is 18 years old for permanent and temporary workers, and all applicants are required to present their age proofs to recruitment staff during the application process.

4.2.c Occupational Health and Safety

All Mercon's operations are fully automated, especially where the highest risks may be present (e.g., wet, and dry mills), so the OHS risks are limited. Nevertheless, Mecon has adopted an OHS Policy (2016) which strongly emphasized its commitment towards risk prevention and zero tolerance to unsafe conditions. This policy is applicable to all workers, contractors (and sub-contractors), suppliers, and visitors.

The Company has progressively established its OHS Management System, including the development of a comprehensive OHS Manual of Standard Operating Procedures (SOPs) – known as “*Normas de Trabajo Seguro*”, including a workplace risk assessment procedure entitled “Hazard Identification and Risk Assessment Control” which included a map of specific occupational risks and its corresponding plan of prevention and promotion of healthy working environment, following the procedure established by the Ministry of Labor (the evaluation was performed by independent evaluators, accredited by the Ministry in November 2015). Each identified hazard was analyzed, according to the level of probability and severity.

Working stations have been designed to optimize safe working conditions, engineering barriers and equipment (e.g., rubber mat at electrical panel location, etc.) have been provided to reduce noise, heat, luminosity, and particle air in suspension while provision of Personal Protective Equipment (PPE) is being provided to all permanent and temporary workers (e.g., overall, helmets, protective boot, and ear plugs) based on workplace risk assessment. In addition, Mercon has established a comprehensive set of SOPs, including work permit system, job competency and training plans to ensure implementation and effectiveness.

The implementation of this OHS management system in Nicaragua is led by an assigned Group-level EHS coordinator with the support of three plant-level OHS supervisors (full-time at San Carlos and La Luz mills). In Honduras, the mill manager is responsible for OHS issues. Each mill has established an OHS Committee (“Commission of Hygiene and Safety”) which define its annual workplan and targets and monitor its effective implementation (e.g., budget, training plan, KPIs, maintenance of internal accident / near-miss register, internal/external audit).

The Company has implemented a comprehensive monitoring and reporting of OHS leading indicators (e.g., safety training, ergonomic opportunities identified and corrected, employee perception surveys, safety audits) and OHS lagging indicators (e.g., injury frequency and severity, OSHA recordable injuries, lost workdays, worker's compensation cost). Also, a procedure “*Reporte e Investigacion de Perdidas y Cuasi perdidas*” is completed for any accident, incident, and near-miss.

Due to the global emergency caused by the COVID-19 pandemic, the Company has also implemented additional technical and administrative OHS measures based on its OHS Management System protocols, including the development of a Manual on COVID-19 Measures, as part of its internal occupational risk prevention services.

4.2.d Workers Engaged by Third Parties

Due to the seasonality of coffee activities, Mercon's operations can involve significant number of directly contracted and sub-contracted workers (e.g., loading / unloading laborers, truck drivers). OHS and HR officers supporting processing and sourcing teams undertake due diligence before establishing a contractual arrangement with an HR labor agency, contractor / service provider, including registration with Ministry of Labor, as well as complying with local labor and OHS provisions, namely payment of worker's legal benefits, timely payment of wages, OHS training and provisions of PPEs.

However, to fully comply with PS-2, the Company will improve its OHS Manual and Procedures to include its due diligence procedure for a contractor's OHS practices and will systematically include HR/OHS provisions in contracts with labor agencies and contractors.

4.2.e Supply Chain

Mercon is in the process of formalizing a Supplier Code of Conduct, which defines the minimum standards that their suppliers shall respect and adhere when conducting business with them on prioritized topics, such as: harmful child / forced labor, lack of fair employment, illegal deforestation, use of banned pesticides, among others. Also, Mercon has already implemented the building blocks of managing supply chain risk assessment, through increasingly sourcing from third-party "sustainability" certified suppliers (when pre-financed), such as Rainforest Alliance (RAF), UTZ, and 4C⁸, and first party regulation (Starbucks Café Program) and Mercon's own E&S Standards (LIFT).

However, to further consolidate the identification and mitigation of supply chain risk, Mercon will undertake a risk assessment for its coffee sourcing in all origins against the "unacceptable practices" defined in the Supplier Code of Conduct mentioned above. This assessment will provide a CAP with its implementation schedule, as necessary.

4.3 Resource Efficiency and Pollution Prevention

4.3.a Resource Efficiency

Mercon is committed to promote efficient resource efficiency through adopting best available technology to achieve energy and water efficiency, implementing robust environmental management practices, and promoting climate-smart interventions (mitigation/adaptation) in its farming, milling and sourcing operations.

⁸ 4C Compliant Coffee is coffee that has been produced in accordance with the 4C Code of Conduct, a set of baseline sustainable practices and principles for the production of green coffee beans. <https://www.4c-services.org/>

4.3.a.i Greenhouse Gases

Wet and dry mill consume significant energy for de-pulping, fermentation, washing, drying and de-hulling processes. Mercon wet and dry mills source its energy from state-owned electricity utility company in all the countries of the Project. To reduce its overall energy consumption and increase its operational competitiveness, the Company has implemented energy efficiencies projects, including more efficient lighting systems (LED), upgrade of compressed air system, installation of translucent roof panels and solar panels at its San Carlos dry mill in Nicaragua. At its wet mill, El Carmen in Nicaragua, the Company installed a methane capture project using biogas for energy production. Finally, coffee husks are being used as feedstock for the ovens, eliminating the need for use of wood.

Mercon has recently started recording its energy (electricity, diesel, petrol, and LPG) consumption. Based on available information in Mercon 2017/2018 CRS, total GHG emissions are estimated to be >25,000 tons CO₂ equivalent annually. Going forward, Mercon will start reporting its GHG emissions annually in its CRS report.

4.3.a.ii Water Consumption

Most of the coffee cherry from smallholders go through an on-site wet mill process for de-pulping, fermentation and washing. Out of its 12 mills, Mercon has only one wet mill (Beneficio El Carmen in Diriamba – processing capacity of this mill is 42 tons/hour). Mercon is promoting the Penagos equipment for wet mills (called machine-assisted wet processing or mechanical demucilaging) as these are leading to significant environmental benefits (e.g., reduction of water usage by 90% compared to traditional “ferment-and-wash method”).

Raw water is extracted from on-site ground water wells. However, to comply with PS-3 and avoid any impact to the water source, the Company will provide hydrogeological studies and develop a Sustainable Water Management Plan for further operation of each well.

4.3.b Pollution Prevention

4.3.b.i Wastes

Wastewater treatment

Main consumption of process water is due to El Carmen’ wet mill (Diriamba, Nicaragua). The facility generates significant volumes of wastewater that contains fermented sub-products (honey water) and other waste from the coffee cherry, characterized by high BOD, high total suspended solids, and acidity. These effluents are stored into well-confined lagoons.

Two main initiatives have been implemented by the Company to address this issue: (i) re-using water from the first cycle into the second washing cycle; and (ii) wastewater treatment, through the project “Energy from Coffee Waste in Central America”⁹. All process waters that cannot be reused is sent to an on-site wastewater treatment plant, which objectives are: (i) produce biogas (methane) that is usable as an alternative energy from the wet method process; and (ii) reduce surface water pollution through effective treatment of wastewater and provide an opportunity for carbon credits. Remaining effluents are stored

⁹ A joint effort funded by the Dutch government and by the Consortium Climate Neutral Group (CNG), UTZ Certified, and CISA.

in an underground reservoir for future use in field application in farms based on strict technical specifications (ref. RFA).

The limited domestic sewage from all operations (mills and warehouses) is collected in septic tanks and treated on-site through a seepage field.

Solid waste

Mercon has adopted a Waste Management Procedure, where its solid waste is characterized (mostly coffee husk, discarded sacks, straps, low-density polyethylene plastic, scrap) and its volume is registered and monitored. Method of reducing, recycling and reuse are being prioritized and documented for all solid waste streams, leaving the elimination or final disposal as last resource. Example, of taking advantage of byproducts are: (i) the coffee husk collected at the dry mills are used as feedstock for the dry mill's ovens; and (ii) the coffee cherries from the wet-mill's de-pulping process are being processed into flour.

4.3.b.ii Hazardous Materials Management

The Company generates very little hazardous waste, mainly in infrastructure maintenance and equipment repair activities. Nonetheless, all its hazardous waste is collected and disposed by a licensed service provider.

4.3.b.iii Pesticide Use and Management

Mercon, through its LIFT's agronomist team, is providing technical assistance to small producers in the selection and use of fertilizers and pesticides with an Integrated Pest Management approach. The Company's supplier use of pesticides is regulated by third-party coffee certification bodies, ensuring that suppliers do not use WHO Class Ia and Ib products as well as products prohibited by the Montreal Protocol (e.g., methyl bromide). Terms and Conditions from local environmental authorities are defined for the safe storage and use of agrochemicals at the farms. Products are fumigated for pest control using aluminum phosphide. Fumigation, when required, is carried out in the warehouses by licensed vendors and in compliance with local regulatory requirements.

4.4 Community Health, Safety and Security

4.4.a Community Health and Safety

Life and Fire Safety

All Mercon operations (farms, mills, warehouses) are maintained as per the local regulations. The farms, mills and warehouses are inspected and certified by the local authorities in compliance with each country's fire prevention standards.

Road traffic safety

Mercon relies on transport service providers during the harvest season for its sourcing of coffee. In Nicaragua alone, more than 1,000 providers are required each year. Therefore, the Company shall define and implement a Road Safety Policy and Procedures in all countries of the Project, with measures to mitigate potential impacts on affected communities based on vehicle composition, for both service providers and their own transport.

4.4.b Security Personnel

Due to challenging security status in Nicaragua, Mercon has hired armed security personnel through a security provider (Vanguard Security S.A. - VSN) for its operations, compliant with the Nicaraguan private security regulations (Law 903 Private Security Services). However, since 2017 the Company has adopted security management practices, defined in the Mercon's Safety and Security Manual for Crisis and Risk Management. This manual includes the determination of the main risks to be addressed in terms of safety, security, and business continuity, and fulfills the criteria for Voluntary Principles on Security and Human Rights (VPSHR), associated to risk assessment practices on security matters.

Also, the Company has established an organizational capacity, led by the Chief of Patrimonial Security, and management structures (including a patrimonial security supervisor and a monitoring center) for such management.

4.5 Land Acquisition and Involuntary Resettlement

Land acquisition and involuntary resettlement do not apply as its farms, milling and sourcing operations has not triggered any physical (resettlement) or economic displacement.

4.6 Biodiversity Conservation and Natural Habitats

4.6.a General

The risk assessment through the IFC's Global Map for risk assessment and management of Agro-Commodity Production (GMAP¹⁰) classified the production and sourcing of green coffee beans in Nicaragua, Honduras, Guatemala and Brazil as medium to high risks (Guatemala and Nicaragua risk assessment for coffee production were not available in the 2018 version of the GMAP) due to well documented labor issues (harmful child labor, forced labor) and/or associated conversion of natural/critical habitats (deforestation). Therefore, Mercon developed and formalized a Supplier Code of Conduct and a Farm Code to eliminate all unacceptable land management practices by Mercon's own operations and third-party supply chains.

4.6.a.i Supply chain

For reputational risk management, as coffee production is associated with medium to high risks from a labor and deforestation standpoint (GMAP), Mercon shall undertake risk assessment of all third-party suppliers in all origins against the unacceptable practices defined in the Supplier Code of Conduct, through: (i) an IBAT risk screening against presence of key biodiversity areas, including critical natural habitats; and (ii) a Forest Loss Risk Index (FLRI, methodology developed by Olam¹¹) to assess deforestation risks in Mercon coffee sourcing catchments areas.

To further consolidate the identification and mitigation of supply chain risk, the Company shall develop a road map to undertake internal risk audit using a range of industry leading third-party risk assessment

¹⁰ www.ifc.org/GMAP

¹¹ Olam Group developed the Forest Loss Risk Index (FLRI) in line with its "Living Landscapes Policy", which is framed around putting more back into food and farming systems than is taken out (<https://www.olamgroup.com/sustainability/policies-codes-standards/living-landscapes-policy.html>)

tools (non-exhaustive) looking at seven materials areas for E&S issues associated with coffee' production in its countries of origin: (i) livelihoods; (ii) land; (iii) water; (iv) climate change; (v) labor; (vi) food security; and (vii) food safety.

4.7 Indigenous Peoples

Within the coffee' production and sourcing catchment areas of the Projects countries, there is no expected presence of indigenous people.

However, both Mercon's Farm Code and Supplier Code, will properly address respecting the rights of local communities and indigenous peoples and their cultural heritage, including Free, Prior and Informed Consent ("FPIC") for new developments.

4.8 Cultural Heritage

Cultural heritage impacts are not foreseen as there is no expected presence of indigenous peoples or known cultural artifacts within coffee' production and sourcing catchment areas.

5. Local Access of Project Documentation

Information of the Company regarding sustainable growth can be accessed at the following link:
<http://merconcoffeegroup.com/home/>

