AUDIT REPORT

CAO Audit of IFC
CAO Compliance

C-I-R6-Y08-F096
June 19, 2009

CAO Audit of IFC's investments in:

Wilmar Trading (IFC No. 20348)
Delta–Wilmar CIS (IFC No. 24644)
Wilmar WCap (IFC No. 25532)
Delta–Wilmar CIS Expansion (IFC No. 26271)

Office of the Compliance Advisor/Ombudsman (CAO)
for the
International Finance Corporation (IFC)
Multilateral Investment Guarantee Agency (MIGA)
Members of the World Bank Group

Acronyms

AMR	Annual Monitoring Review
AMRR	Annual Monitoring Review Report
BACP	Biodiversity and Agricultural Commodities Program
BTO	Back-to-Office Report
CAO	Office of the Compliance Advisor/Ombudsman
CAP	Corrective Action Plan
CES	IFC's Environmental and Social Department
CIC	IFC's Corporate Investment Committee
CPO	Crude palm oil
CSO	Civil society organizations
EIA	Environmental Impact Assessment
ERS	Environmental Review Summary
ESRP	Environmental and Social Review Procedure
FFB	Fresh fruit bunches
FWI	Forest Watch Indonesia
GEF	Global Environment Facility
GFW	Global Forest Watch
ha	Hectares
IEG	Independent Evaluation Group
IFC	International Finance Corporation
MAM	Management Approval Memorandum
MIGA	Multilateral Investment Guarantee Agency
NES	Nucleus Estate and Smallholder program
NGO	Non-governmental organization
OED	Operations Evaluation Department (World Bank)
PKO	Palm kernel oil
PS	Performance Standards
PTP	Perseroan Terbatas Perkebunan (state-owned agricultural enterprises)
RSPO	Roundtable on Sustainable Palm Oil
SPI	Summary of Proposed Investment
WBG	World Bank Group

Definitions

Inti	nucleus estate
Plasma	participating farm household

The overall objective of the compliance audit is to assess the reasonableness of IFC's approach to these investments based on its mission, policies, standards, experience, and guidance. This includes an assessment of:

Whether the current procedures and established practices provide sufficient and correct guidance to IFC staff in assessing upstream supply chain issues to ensure that the outcomes of the investments made meet the intent of applicable policies, as well as IFC's mission and mandate.

How IFC assured itself that these investments would achieve an outcome consistent with IFC's development mission, and how, during its review process, IFC considered earlier experiences of achieving sustainable development outcomes within the region, country, sector, and with the client.

Whether the allocation of Category 'B' and 'C'[1] to these investments was reasonable, taking into account the specifics of the sector, the region, and earlier experiences.

Whether the allocated categorization was consistent with IFC's environmental and social policies and standards at the time of the different investments.

Whether IFC's rationale for defining the upstream supply chain as not associated with, and outside the area of influence of their investments was reasonable and correct, taking into account IFC's policies, mandate, and mission.

The scope of the audit also includes developing an understanding of the immediate and underlying causes for any non-compliance identified by the CAO.

The scope of CAO Compliance appraisals and audits is limited to the issues raised in the request, and related to the complaint. The CAO cannot accept an expansion of the scope defined in the request, or expand beyond issues related to the complaint.

A major underlying issue of concern for the CAO is how sustainable livelihoods are achieved, or secured, for the people impacted by IFC's investments.

Specific complainant concerns

The complainants further specified their concerns with respect to alleged violations of IFC Performance Standards and Safeguard Policies[2] in several particular contexts: compliance with applicable national laws, including host country obligations under international law; analysis of social and environmental risks and impacts in a Social and

[1] Categorization as defined in IFC's "Environmental and Social Review Procedures", http://www.ifc.org/
CATEGORY 'A': Projects expected to have significant adverse social and/or environmental impacts that are diverse, irreversible, or unprecedented. **CATEGORY 'B'**: Projects expected to have limited adverse social and/or environmental impacts that can be readily addressed through mitigation measures. **CATEGORY 'C'**: Projects expected to have minimal or no adverse impacts, including certain financial intermediary projects.

[2] http://www.ifc.org/

For this audit, as with all CAO audits of IFC, the objective is to provide greater clarity in relation to the steps that IFC took, or did not take, to assure itself of the performance and impacts of its investments. The overall scope is to assess IFC from a perspective of compliance with audit criteria related to the allegations put forward in the complaint. As part of the audit, the CAO seeks to develop an understanding of the causes for any non-compliance identified, which includes both the immediate causes and any underlying causes.

1. Overview and Background Relevant to IFC's Investments

The four IFC loans to Wilmar that are the focus of the CAO audit and this audit report have their roots in the development pattern of the oil palm industry in Indonesia. This brief background section introduces these topics, starting with a description of palm oil and its production in Indonesia (see box 1).

Box 1. Palm Oil and Products

Palm oil is derived from the fruit of the tropical oil palm, which originated in West Africa. Oil palms are grown for their multiple clusters of fruit, called fresh fruit bunches (FFB), which can weigh 40–50 kg each. Yields, which are highly dependent on sound agronomic practices and soil fertility, commence about 3 years after planting and peak after 5–10 years. The palms require replanting after approximately 25–30 years. In Indonesia, Malaysia, Papua New Guinea, and other countries, oil palms are cultivated by small farmers and by plantations. Fresh fruit bunches are harvested throughout the year and are processed within 24 hours into crude palm oil (CPO) and palm kernel oil (PKO) at mills located near cultivated areas.

Typically, plantation companies own these mills and process their own fruit and fruit from smallholders under contract. CPO/PKO is used to produce a range of products including edible oils, cooking fats and soaps, and biofuels. Further refining and fractionation of CPO/PKO yields a wide range of higher value products (for industrial products and cosmetics, for example), and may take place in the producing country or be shipped for processing closer to end-product markets.

Global demand for CPO/PKO and derivative products is currently strong, and is expected to remain so, especially for cooking oil in major emerging markets, and for biofuels in developed markets. Indonesia and Malaysia have a strong comparative advantage and dominate world production and trade due to suitable growing conditions and cost factors.

1.1 Oil palm in Indonesia

Despite being introduced in Indonesia in 1848, oil palm was first cultivated in North Sumatra in 1875. Oil palm was grown only on plantations—unlike rubber, which developed strong support from small farmers in the early years. Large-scale cultivation began in 1911 in North Sumatra and Aceh, and by 1938 the area cultivated was close to 100,000 hectares (ha). Stagnation occurred in the 1940s and the Indonesian government nationalized all foreign-owned estates between 1958 and 1960. A decade later, the policy of nationalization was reversed.

In the 1960s and 1970s, Indonesia relied heavily on agriculture and to a lesser extent on forestry and fishing. With 80 percent of the country's 135 million people living in rural areas, the sector dominated the life and welfare of the Indonesian people. Rice contributed 30 percent of agricultural GDP and supply was growing slowly, as was the supply of other food crops. The main rural problems related to overpopulation, small farm size, and low productivity. The best soils are in Java, Madura, and Bali, all of which had intensive cultivation, and even marginal land was cultivated. On Java, one-third of the agricultural labor force was landless, and 40 percent of farm incomes were derived off-farm. With a rising population, the future looked bleak.

To address rural problems, the government's Second Five Year Plan (1974–9) listed its priorities as employment creation, balanced regional growth, social development, increased food crop production, and increased export crop production—especially rubber, to maintain Indonesia's market share. Strategies to support this accelerated land settlement included transmigration to bring some of an estimated 40 million hectares of "unutilized land", mostly on the outer islands, into smallholder food crop and tree crop production, plus a replanting program for rubber and coconut. The establishment of rural livelihoods based on oil palm development and other industrial tree crops was an important part of the government's strategy.

The early years of the Suharto era (1967–98) strengthened the role of the state and promoted state-owned agricultural enterprises (*Perseroan Terbatas Perkebunan*, or PTPs). These companies and private plantations were encouraged to plant large-scale oil palm as well as other industrial tree crops such as rubber, coconut, and tea. For oil palm, the government's intention was to ensure adequate supplies of affordable cooking oil for domestic consumers, promote industrial development, and boost non-oil exports.

In view of scarce technical and managerial capabilities, one of the main approaches selected by the government was to use the PTP corporations to plant tree crops on land to be settled by local landless families and transmigrants. The companies provided a range of services, including planting material, land clearing and planting, and procurement of inputs, and provided processing and marketing facilities to the smallholders. The World Bank and other major donors such as the Asian Development Bank (ADB) were invited by the government to assist in financing Nucleus Estate Smallholder (NES) projects and other projects that were based on the development of industrial tree crops.

1.2 WBG and NES programs

Smallholder involvement in oil palm cultivation was strongly promoted in the 1970s, which included support through seven World Bank/IDA loans under the Nucleus Estate and Smallholder (NES) program. Under the NES concept in Indonesia, a state-run or private-run company became the nucleus estate (*Inti*) of the system, and each smallholder (*plasma*, or participating farm household) was allocated 2 hectares per household for cultivation and 1 hectare for housing. Smallholders came from the area or were resettled from other areas.

The NES projects were implemented through a contractual arrangement between financial capital and technical expertise (for example, through a PTP's financial and technical resources, external loans, and government funds), human resources (for example, by settling landless people or villagers whose living conditions and skills were anticipated to be significantly improved), and available ("unutilized") land for perennial crop and food crop cultivation. The NES projects were expected to generate productive employment at relatively low cost and raise farm incomes of landless and near-landless families. The tree crops under the World Bank NES program were oil palm, rubber, and coconut, which accounted for significant shares of agricultural GDP and non-oil exports, as well as food crops. Other development agencies, including the ADB, Commonwealth Development Corporation, Gesellschaft Technische Zusammenarbeit (GTZ), and the International Fund for Agricultural Development, also supported projects under the NES program.

The World Bank-financed NES projects are well documented and have been the subject of analysis. Hundreds of thousands of rural jobs were created through the expansion of tree crops, especially in the eastern part of Indonesia, where poverty was of high concern. Tree crops grown on NES projects played an important role in poverty reduction, particularly where soils were not suitable for annual crops. However, the World Bank Group's overall assessment in the 1992 Operations Evaluation Department (OED) Report and the Project Completion Reports of various loans was that the NES style of investment through the PTPs in the 1970s and 1980s had not met its goals. For instance, an OED evaluation of three projects —NES IV, V, and VI—notes that "a more gradual approach, on a smaller scale, might have left more sustainable benefits. The projects overstretched the management capacity of the public sector estate companies that were responsible for implementation. Most of the public sector estate companies lacked financial flexibility and were vulnerable to delays and reductions in the funds released for the projects from the government budget".[3]

The 1989 World Bank strategy that replaced the earlier approach called for greater private sector involvement, gave greater emphasis to the legal and policy framework, governance, and building institutional capacity. At that time, concerns over deforestation were emerging and rights over forest resources were becoming a major issue of social dispute. Burning of vegetation to facilitate the conversion of forests, grasslands and peat soil areas into oil palm plantations, as well as the resulting loss of habitat and biodiversity, led to international concerns. The oil palm and timber plantation companies were found to be mainly responsible for the massive forest fires in Indonesia in 1997 that contributed to regional smog and health risks in neighboring countries (see box 2).

Box 2. Forest Losses in Indonesia and the Role of and Impact on Smallholders

International comparisons show that QGRQHVLD¶V UDWH RI IRUHVW ORVV LV D
Several World Bank reports argue that in the last two decades, in Indonesia at a national scale,
industrial/large-scale impacts on forests have outweighed the effects of smallholders [illegible].

[3] "Nucleus Estates and Smallholders Projects in Indonesia – Performance Audit Report", OED, World Bank, September 1992.

A joint World Bank and IFC report[4] cites[5] data supporting the conclusion that smallholder expansion of cultivated areas for food crops and cash crops does not appear to be a primary encroachment.[6] Of the crops examined (clove, coconut, coffee, oil palm, rubber, sugar cane, tea, and tobacco) only oil palm has seen a major expansion since the early 1990s.[7] Although forest degradation and loss involves many actors and many causes, and smallholders play a role, the report concludes that commercial expansion of oil palm estates has been more serious than smallholder incursions in recent times. In terms of the underlying causes of deforestation, Global Forest Watch (GFW)/ Forest Watch Indonesia (FWI)[8] mentions governance issues, including unclear legal status of land, inappropriate land use allocations, weak enforcement, land conflict, industrial overcapacity, poverty and landlessness, and regional government revenue needs.

The World Bank report also highlighted weak incentives for sound and sustainable forest management and noted that licenses have been granted for timber harvesting and conversion of forested lands into plantation crops. Acts of short-term opportunism had also occurred, with some licensees focusing on harvesting timber, rather than long-term plantation development. “The land c granted from the centre, may also displace local communities or constrain their livelihood opportunities on traditionally used areas,” the World Bank report notes. Overall, the existing incentives favor continued plantation development over smallholders, the World Bank report concluded.

1.3 Private sector development of oil palm

Since the late 1980s, private estates have played an increasingly important role in oil palm expansion. By the late 1980s, the World Bank and most other donors that supported the NES schemes had reached the conclusion that investments via public sector tree crop corporations (PTPs) were not suitable for further smallholder developments. By 1989, the World Bank was advising that “The public sector estates companies (PTPs) succeeded in planting large areas for smallholders, but now face major debt servicing obligations and operational inefficiencies….the PTPs will need to return to their role as commercial enterprises…”.[9]

As outlined in the 1989 strategy, the World Bank then saw the private sector as the major driver for growth. Private sector oil palm development accelerated rapidly in the 1990s and by 2002, over half the planted area of 4.1 million hectares was owned by private companies, 30 percent by smallholders, and 13 percent by state-owned companies. By 2005, the area planted had expanded to over 6 million hectares. Many private companies used forestry exploitation to help defray the cost of plantation development or as a primary objective to earn revenue.

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[4] “Sustaining Economic Growth, Rural Livelihoods and Environmental Benefits”, World Bank, 2006.
[5] World Bank report cites Minister of Agriculture, Area and Production of Estate Crops, 1993 to 2002.
[6] “Sustaining Economic Growth, Rural Livelihoods and Environmental Benefits”, World Bank, 2006.
[7] Cocoa, if included, would have had an impact.
[8] “The State of the Forest: Indonesia”, Forest Watch Indonesia and Global Forest Watch, Washington DC, USA, 2002.
[9] “Indonesia: Strategies for Sustained Development of Tree Crops”, World Bank, 1989 and “Indonesia: Strategies for Sustained Development of Tree Crops, World Bank, 1989, Volume II”.

IFC debated the social and environmental issues involved and agreed to pay extra attention to these in the AMRRs.

Overall, AMRRs, BTOs, CAPs, and the ERS record numerous problems and slowness in alleviating or mitigating the concerns at the project level. A 2006 IFC study of the palm oil value chain in Aceh identified the following issues of concern: poor returns to smallholders, lack of access to services, and the need for improved industry environmental management and better interaction with local communities.

1.5 Development of the Wilmar Group

Wilmar International Limited was founded in 1991 as a joint partnership between a Malaysian national, Mr. Kuok Khoon Hong, and an Indonesian national, Mr. Martua Sitorus. It commenced operations as a palm oil trading company.

Besides his engagement and ownership in Wilmar, Mr. Kuok has interests and close relationships with the Kuok Group, a Malaysian-based agribusiness conglomerate. In 2007, Wilmar bought the Kuok Group's palm plantation business, increasing Wilmar's planted oil palm acreage and land bank. In addition to his engagement and ownership in Wilmar, Mr. Martua Sitorus has interests in and a close relationship with Ganda Group Indonesia, an Indonesian plantation-operating group. The CEO and President of Ganda Group, Mr. Ganda and Mr. Sitorus, respectively, were involved in the establishment and management of PT Karya Prajona Nalayan (PT KPN), which became part of Wilmar International Limited.

Wilmar explains on its public web site and in its annual reports: "Over the years, we have established a resilient integrated agribusiness model that captures the entire value chain of the agricultural commodity processing business, from origination and processing to the branding, merchandising and distribution of a wide range of agricultural products. Through scale, integration and the logistical advantages of our business model, we are able to extract margins at every step of the value chain, resulting in significant operational synergies and cost efficiencies".

In 1991, when Wilmar started engaging in the merchandising of palm oil in Indonesia, it acquired a land bank of approximately 7,100 hectares in Western Sumatra. By 2002, the plantation area was stated to have reached 80,000 hectares.

In 2006, Wilmar announced a proposed merger with the Kuok Group's palm plantation, edible oils, grains, and related businesses (PGEO Group Sdn Bhd and PPB Oil Palms Berhad) in a deal worth up to US$2.7 billion. In a separate transaction, Wilmar announced a restructuring exercise to acquire the edible oils, grains, and related businesses of parent company Wilmar Holdings Pte Ltd, including interests held by Archer Daniels Midland Asia Pacific and its subsidiaries in these businesses, for US$1.6 billion. The company was renamed Wilmar International Limited on July 14, 2006, upon completion of the reverse takeover of Ezyhealth Asia Pacific Ltd. In 2006, Wilmar also concluded a major production capacity expansion drive through the completion of three refineries, three fractionation plants, four palm kernel crushing plants, and four palm oil milling plants. In parallel, Wilmar expanded its oil palm plantation acreage through the acquisition of five plantation companies (with a combined land bank of 85,000 hectares in Kalimantan, Indonesia), the acquisition of 25,000 hectares of land bank by two existing subsidiaries, and the acquisition of a plantation company with a land bank of 30,000 hectares in Jambi, Sumatra.

As of 2008, Wilmar was one of the world's largest processors and merchandisers of palm and lauric oils, and one of the largest plantation companies in Indonesia/Malaysia. The assets of the Wilmar Group were valued at US$17 billion. A net profit of US$1.53 billion was reported (Wilmar 2008 Annual Report). In Indonesia, its plantations are located in Sumatra, West Kalimantan, and Central Kalimantan (southern region), while in Malaysia, they are located in the states of Sabah and Sarawak. As of December 31, 2008, Wilmar owned approximately 570,000 hectares of plantation land, of which 223,000 hectares were planted, according to its 2007 and 2008 Annual Reports.

Wilmar states that it intends to grow its plantation business through greenfield projects and acquisitions. Total planted area is expected to triple within a decade through new plantings of about 40,000 hectares per year.[14]

1.6 Development of RSPO

In 2001, the World Wildlife Fund (WWF) initiated an exploration of the possibilities of forming a voluntary international organization to establish sustainable practices in the palm oil sector. In 2004, the Roundtable on Sustainable Palm Oil (RSPO) was formally established.

RSPO is composed of Ordinary Members in seven different sectors—oil palm growers, palm oil processors and/or traders, consumer goods manufacturers, retailers, banks and investors, environmental/nature conservation NGOs, social/developmental NGOs—as well as Affiliate Members. It currently has over 250 Ordinary Members and close to 100 Affiliate Members.

The objective of the RSPO is to become the central body for allowing certification of sustainable palm oil. To this end, it has adopted eight principles:

- Principle 1. Commitment to transparency
- Principle 2. Compliance with applicable laws and regulations
- Principle 3. Commitment to long-term economic and financial viability
- Principle 4. Use of appropriate best practices by growers and millers
- Principle 5. Environmental responsibility and conservation of natural resources and biodiversity
- Principle 6. Responsible consideration of employees and of individuals and communities affected by growers and mills
- Principle 7. Responsible development of new plantings
- Principle 8. Commitment to continuous improvement in key areas of activity.

[14] Wilmar International Ltd., 2007 Annual Report, page 2.

2.2.11 The CAO finds that IFC's decision to exclude the palm oil supply chain contradicts Wilmar's stated business strategy.

2.2.12 The CAO finds that IFC's stated inability to trace CPO to specific plantation areas in Indonesia is incorrect and is therefore not a valid argument for excluding a supply chain with social and environmental concerns that are well documented. The CAO finds this inconsistent with the intent of IFC's policies and mandate.

2.3 RSPO

2.3.1 In 2005, RSPO was a newly formed, member-regulated industry association. IFC notes that the establishment of the RSPO was an important consumer-driven development, and that Wilmar became a member and supported the RSPO principles.

2.3.2 The CAO finds that Wilmar's stated support of the RSPO principles cannot substitute the application of IFC's policies, procedures, and standards. The IFC's Performance Standards are more comprehensive, and provide safeguards in areas that the RSPO principles do not address. RSPO had no established independent verification process in operation to verify performance on the ground at the time of the investments.

2.4 Technical assistance

2.4.1 IFC recognized that poor management practices in the palm oil supply chain were a reputational risk. In response, in 2006, IFC proposed and started to developed a technical advisory program intended to promote sustainable practices along the supply chain and to mitigate in part the reputational risk of the proposed investments in Wilmar. IFC stated that this program would provide tools to improve traceability, address supply chain issues, and introduce incentives related to those smallholders from which Wilmar obtained CPO.

2.4.2 The CAO finds that as of 2009, only one limited scope technical advisory project had been approved. A small grant (US$ 211,000) to the London Zoological Society, in association with Wilmar and financed by the Global Environment Fund (GEF) under the Biodiversity and Agricultural Commodities Program (BACP), seeks to address biodiversity concerns.

2.5 IFC No. 25532–Wilmar WCap (2006)

CIC Review, October 26, 2006; Investment Review Meeting, November 30, 2006; Board approval, December 20, 2006; Commitment, February 9, 2007.

IFC states: "The project is intended to enable Wilmar Trading Pte Limited…, to meet its working capital needs to purchase crude palm oil (CPO) from palm oil plantations in Indonesia and process them into refined oil for export. IFC's support is essential to enable the company to finance its export program and allow continued sustainable long-term growth in a sector where Indonesia has a strong comparative advantage and will be a good illustration of IFC's support for good sponsors in a socially sensitive sector. The project will ensure the continuous operation of the CPO supply chain and the preservation of all economic interests and employment associated with that chain such as plantation, transportation, storage, processing and shipping."[18]

The investment in the Wilmar trade facility (Wilmar WCap, IFC No. 25532) was reviewed according to the 2006 Environmental and Social Review Procedure (ESRP) and the 2006 IFC Performance Standards.

2.5.1 IFC assessed the performance of a small sample of Wilmar plantations in some detail as part of its due diligence review.

2.5.2 IFC attached significance to Wilmar's membership of the RSPO with regard to social and environmental issues.

2.5.3 IFC was aware of well-documented civil society concerns about the sustainability of plantation development and operations in West Kalimantan.

2.5.4 IFC's Summary of Proposed Investment (SPI) focuses on Wilmar's ability to manage the palm oil supply chain and to extract value from it.

2.5.5 IFC Performance Standards state that adverse impacts associated with supply chains shall be considered where low cost labor is a factor, or where the resource utilized is ecologically sensitive.

2.5.6 IFC Performance Standards state that where the client has commercial leverage over its suppliers, IFC will expect the client to work with its suppliers to propose mitigation measures to increase their performance.

2.5.7 IFC categorized this second investment in the trade facility as a Category 'C' project, the same as its categorization of the first Wilmar trading investment. The decision was again based on IFC's argument that as a trade facility, the project would have limited, or no, environmental or social impacts. It therefore excluded the supply chain from its investment decision making process.

2.5.8 The CAO finds that both impacts on low cost labor and ecologically sensitive resources are directly relevant to the palm oil sector.

2.5.9 The CAO again finds this categorization inconsistent with IFC's policy and procedural provisions.

[18] Summary of Proposed Investment (SPI) for IFC No. 25532.

the Wilmar Group, and the challenges that existed within the Indonesian palm oil sector.

2.8 Compliance with National Laws

2.8.1 IFC did not assess the Wilmar plantation operations compliance with national laws in its due diligence of its Wilmar projects, since IFC decided to exclude the plantation operations from the scope of the due diligence

2.8.2 The CAO finds that in November 2007 and January 2008, IFC and Wilmar acknowledged shortcomings in how its policies were applied on the ground. This included acknowledgment of failure by the plantation operations to comply with national legal requirements related to permits and standards, and disclosure of environmental impact assessments (EIA).

2.8.3 Because IFC excluded legal compliance of the plantation operations from its due diligence reviews, IFC failed to identify legal non-compliance issues.

3. CAO Conclusions

3.1 Observation

3.1.1 The CAO concludes that IFC had no specific strategy that provided guidance for engagement in the Indonesian palm oil sector, despite the recognized social, environmental, and governance sensitivity of the sector, prior IFC and WBG experience, and IFC's own recognition of the significance of its engagement in the sector.

3.1.2 The CAO concludes that, from a due diligence perspective, IFC's environmental and social review procedures do not adequately address the particular characteristics of trade financing, or other similar kinds of investments. At present, there is no procedure implemented for such investments that addresses the sector, country and commodity based risks.

3.1.3 The CAO concludes that the difference in scope of environmental and social reviews for a category 'A' or 'B' project, versus a category 'C' project is considerable. As a result, IFC is exposed to the possibility that significant internal and external commercial pressure is placed on IFC's categorization process to decide a Category 'C' result.

3.2 Non-compliance Issues

3.2.1 The CAO concludes that IFC did not meet the intent or the requirements of the Performance Standards in its assessment of the Wilmar trade facility investment (Wilmar WCAP, IFC No. 25532), and that the project should not have been categorized as 'C'. The 'C' categorization led to an assessment that was too narrow in its scope and too limited in its execution, and that in turn failed to trigger assessment of applicable Performance Standards.

3.2.2 The CAO concludes that the IFC assessment of Delta Wilmar CIS Expansion (IFC No. 26271) failed to take into account the supply chain plantations and other companies and suppliers linked to the Wilmar Group, as required in the Performance Standards. This led to a scope of IFC's due diligence that was too narrow and limited, and that in turn failed to trigger assessment of applicable Performance Standards.

3.2.3 The CAO concludes that this narrow interpretation of the investment impacts—in full knowledge of the broader implications—was inconsistent with IFC's asserted role, mandate and commitment to sustainable development.

3.3 Underlying Causes for Non-compliances Identified

3.3.1 Commercial pressures were allowed to prevail and overly influence the categorization and scope and scale of environmental and social due diligence in the Wilmar Group investments. As a result, IFC's development mandate and mission were not robustly represented in the decision-making processes.

3.3.2 The significant differences between the social and environmental due diligence approaches for a Category 'A' and 'B' project versus a Category 'C' project create pressure on IFC both internally and externally to structure an investment so that it falls within the Category 'C' range.

3.3.3 Incorrect assumptions were made about the impact of certain types of financial products (trade facilities) without proper consideration of the sector and country context of the investment. IFC should not have assumed that a trade facility project would be a Category 'C' without appropriate screening of the full context of the investment. IFC should have considered the impacts of its investment, rather than a narrow interpretation of specific financial flows.

3.3.4 IFC paid inadequate attention to civil society monitoring reports and concerns about continuing social, environmental, and economic problems in the oil palm industry in Indonesia.