IFC | International Finance Corporation
WORLD BANK GROUP

March 3, 2016

Mr. Osvaldo L. Gratacós
Compliance Advisor Ombudsman
International Finance Corporation
2121 Pennsylvania Avenue, N.W.
Washington DC 20433

IFC Management Response to the CAO Investigation Report on Delta-Wilmar 03/Jambi (#25532 and #26271)

Dear Mr. Gratacós:

IFC Management appreciates the opportunity to respond to this 2016 CAO Investigation Report pertaining to IFC's performance with respect to its former client, Delta Wilmar. This latest audit, reviewing supply chain supervision during the 2010-12 period of two IFC investments in a Ukrainian refinery, overlaps substantively with the 2009 CAO audit of IFC investments in Wilmar. Given the overlap, the key findings of both audits note that a more rigorous and systematic approach in due diligence and supervision of the palm oil supply chain was warranted. As in 2009, IFC acknowledges this core finding. However, as you are aware, our policies and practices today are far different and more advanced, with many improvements developed and put in place, subsequent to the 2009 audit. These improvements are as responsive to the findings of the 2016 audit as they were to the 2009 audit.

New IFC Approach to High Risk Commodity Supply Chains

IFC's new approach, catalyzed by the 2011 strategy for palm oil-related investments, includes more rigorous Performance Standards requirements and comprehensive environmental and social risk screening tools (such as GMAP, which is now widely used by most Development Finance Institutions and Equator Banks). In addition, IFC developed a *Good Practice Handbook for Agro-Commodities Risk Assessment and Management* that outlines a methodological approach to identifying and mitigating supply chain risks. This approach applies systematically to all IFC investments triggering Performance Standard supply chain requirements. Additionally, there are new screens and measures in place to guide prospective IFC direct investments in palm oil. These include, for example, an Integrated Biodiversity Assessment Tool and GIS mapping process, as well as High Conservation Value assessments by credible third parties. IFC also undertakes, in collaboration with the World Bank, a Country Situation Analysis prior to considering any new palm oil investment in a particular country. These tools collectively provide IFC with key insights into project-related risks and contextual risks, including those related to supply chains.

The Loan Agreement and Decision to Disburse

In reviewing the 2010-12 period covered by the 2016 CAO investigation, it is important to recall the historical context and events that materially influenced IFC's decision-making and approach to addressing palm oil supply chain issues. As both CAO investigation reports indicate, IFC approached the investment as a stand-alone project financing for the Delta Wilmar refinery in Ukraine. It was IFC's judgment at the time that the Performance Standards, with respect to supply chain provisions, were not triggered because the refinery had limted influence over environmental and social management practices applying to primary fresh fruit bunch production in Indonesia or elsewhere. The absence of a long-term supply contract between Wilmar's palm oil plantations and Delta Wilmar was a key factor in making this judgment. As a result, there were no specific conditions of disbursement referencing supply chains incorporated into the loan agreement which was finalized and signed in November 2008 (prior to the 2009 CAO audit and the subsequent IFC Management Response/Action Plan).

Two contextual realities were particularly important in defining IFC's options and decision-making. First, despite attempts, IFC did not have sufficient leverage with Delta Wilmar at the time of disbursement in January 2010 to address supply chain issues. Delta Wilmar was only partially owned by Wilmar and sourced its crude palm oil from multiple sources. Second, IFC also took into consideration the ongoing CAO effort to seek a mediated solution to the complaints by local communities and sought to ensure the continuation of an influential and productive relationship with Wilmar. Wilmar had already recognized the benefit of a previous successful CAO mediation and had embraced CAO's help in trying to solve the land dispute underlying the 2008 Jambi complaint. Withholding disbursement in early 2010, while trying to retrofit new environmental and social requirements, was an impractical course of action to pursue and would likely have adversely affected the ongoing CAO mediation.

Nevertheless, IFC acknowledges that inclusion of the 2006 Performance Standards in the Delta Wilmar loan agreement obligated IFC to develop a more robust approach to addressing palm oil supply chains relevant to the refinery. At the time of the January 2010 disbursement, efforts to address palm oil supply chain and other sustainability issues were being pursued outside the Delta Wilmar loan agreement. These measures, including the well-documented World Bank Group commitment and process to reformulate its approach to the palm oil sector, represented the most practical approach to addressing many of the issues raised in this and the 2009 CAO report.

Progress Achieved since 2009

From 2009, there was a wide range of collaborative efforts undertaken by IFC to work with Wilmar to address the environmental and social performance of the company's palm oil production facilities in Indonesia. This work with the client at a corporate level in support of better environmental and social performance is an important part of IFC's role. Our engagements with Wilmar during the period covered by the investigation contributed to the company's decision to sign on to the *Indonesia Palm Oil Pledge*. This "pledge" commits the company to no deforestation, no planting on peat, and avoidance of social conflict in their own palm oil operations. In addition, the company is in the process of implementing a policy to no longer purchase fresh fruit bunches or crude palm oil from third-party suppliers who do not adhere to this pledge.

The totality of IFC's action plan in response to the 2009 audit delivered greater impact and reach than would have a more narrowly focused approach anchored in a loan agreement for a joint-venture Ukrainian refinery. IFC also engaged directly with Wilmar since the parent company clearly had more influence over its own plantations and its fresh fruit bunch/crude palm oil supply chain. IFC engaged directly with Wilmar's Sustainability Manager to assess progress of Wilmar's certification of its plantations, mills and third-party suppliers during the period in question.

Wilmar's already existing commitment to seek RSPO certification of its own plantations in Indonesia, and sustained progress over many years in this regard, demonstrated its commitment to being a sustainability leader and advocate within RSPO. Equally, Wilmar recognized the need for continuous improvement in its practices. IFC–as the CAO investigation notes–took additional comfort from this evidence-based commitment on the part of its client. It is noteworthy that Wilmar has now achieved 87% RSPO certification of its own plantations in both Indonesia and Malaysia.

Conclusion

It is worth recalling the related events and realities of the time period, including: (a) CAO's own constructive and ongoing relationship with Wilmar related to the second CAO complaint and the delicate nature of that relationship, given the existing sensitivities associated with the 2009 audit; (b) the World Bank Group Palm Oil Strategy process, which was just getting underway to guide all future investments in the sector (and incorporating extensive consultations in Indonesia with those complainants and stakeholders directly impacted by Wilmar operations); (c) the procedural changes IFC had already made, or was in the process of making, to correct past gaps associated with palm oil/Wilmar investments; (d) how the Wilmar experience was informing the strengthening of the Performance Standards (incorporating further supply chain provisions) reflected in the 2012 iteration; (e) the significance of Wilmar's ongoing commitment to achieve RSPO certification for its Indonesian plantations; and (f) the explicit commitments made in the 2009 Management Action Plan, including an independent environmental and social review of a representative sample of Wilmar plantations. CAO's compliance monitoring reports for the 2009 Action Plan acknowledged that IFC had fulfilled this commitment by virtue of a third-party assessment and associated Environmental and Social Action Plan.

In sum, IFC now handles due diligence and supervision of supply chain issues, and specifically investments in the palm oil sector, much differently and better than was the case during the period covered by the 2009 and 2016 reports. This progress can be credited, in part, to the transformative impact of the 2009 CAO audit. However, because this current investigation revisits a time period that predates these advancements, and substantively covers much of the same ground on supply chain issues, it duplicates much of the previous 2009 audit. IFC Management looks forward to ongoing engagement with CAO to promote a better use of our collective resources and to help ensure that improvements in our diligence and supervision continue to be implemented. The Corporation is committed to maintaining its leadership in promoting sustainability in agricultural supply chains.

Sincerely,

Ethiopis Tafara
Vice President and General Counsel
Corporate Risk & Sustainability

Dimitris Tsitsiragos
Vice President
Global Client Services