Palm Oil and the Importance of Participation in Sustainability Regulatory Schemes

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Abstract

This paper focuses on three regulatory standard setting schemes: the Performance Standards for environmental and social performance (Performance Standards) published by the International Finance Corporation (IFC); the Equator Principles; and the Roundtable on Sustainable Palm Oil (RSPO). Two palm oil case studies show how the IFC’s Compliance Advisor Ombudsman (CAO) and nongovernmental organizations (NGOs) promote, with mixed success, the responsiveness of the IFC to people affected by projects it supports.

The first case concerns IFC investments in the Wilmar Group, which were connected to Wilmar’s oil palm plantations. The CAO’s June 2009 compliance audit report criticized the IFC’s supply chain assessment in light of its Performance Standards, and prompted development of an IFC palm oil sector strategy. World Bank Group palm oil investments were suspended pending development of the strategy. Similar complaints regarding Wilmar to the RSPO received a weak response in which the RSPO aimed to resolve disputes without making adverse findings against Wilmar.

The second case concerns the IFC’s April 2009 loan agreement with Corporación Dinant (Dinant) in Honduras for oil palm plantations, amongst other things. Dinant was allegedly connected to violent evictions of farmers following a military coup in June 2009, yet the IFC executed the first disbursement five months later. The Wilmar case shows how transparency and review measures facilitate the enforcement activities of NGOs and the CAO, which involve interactions with the IFC that set the standards and influence reviews of the Performance Standards. The case studies also demonstrate the relative weakness of the RSPO complaints mechanism, and the lack of transparency under the Equator Principles.

The paper argues that the Equator Principles need transparency and review to promote responsiveness to project-affected people whose interests the Principles claim to uphold. The paper also argues that the IFC must advocate for such

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responsiveness-promoting measures to ensure its legitimacy as a promulgator of sustainability standards.
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1. Introduction

This paper argues that transparency and review measures are important for the governance of sustainability standards because such measures promote responsiveness to project-affected people by enabling participation in regulatory standard setting schemes for sustainability standards. The paper considers two palm oil industry case studies for the three schemes considered by the paper: the Performance Standards for environmental and social performance (Performance Standards) published by the International Finance Corporation (IFC); the Equator Principles; and the Roundtable on Sustainable Palm Oil (RSPO). The palm oil case studies indicate that there is significant potential for nongovernmental organizations (NGOs) and review bodies to influence a regulatory scheme through grievance mechanisms, promoting responsiveness to project-affected people whose interests might otherwise be disregarded. The palm oil case studies also suggest that such influence is not possible in the RSPO scheme due to institutional reluctance to make adverse findings or rigorously monitor compliance following complaints. The case studies highlight the Equator Principles’ lack of transparency, and this paper argues that the Equator Principles need transparency and a grievance mechanism to improve Equator Principles Financial Institutions’ responsiveness to project-affected people, whose interests the Principles claim to address. The paper also argues that the IFC must champion such responsiveness-promoting measures to ensure its legitimacy as a promulgator of sustainability standards such as the Equator Principles.

The IFC Performance Standards, Equator Principles, and RSPO are examples of regulatory standard-setting (RSS) schemes. RSS schemes are non-state and public-private governance arrangements with norms that address social and environmental issues.\(^\text{1}\) Abbott and Snidal have identified five activities in the “regulatory process” of RSS: agenda-setting, negotiation of standards, implementation, monitoring, and enforcement.\(^\text{2}\) Different measures based on global administrative law (GAL) principles can enable or enhance different steps in regulatory processes, making an RSS scheme more responsive to otherwise disregarded interests.

GAL is an emerging area of international law that concerns the accountability of actors and institutions that hold power in international governance, and the responsiveness of these actors and institutions to those whose interests are affected by their power.\(^\text{3}\) A key problem identified by Stewart that GAL seeks to address is the problem of the “disregarded”—those whose interests are affected by

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\(^{2}\) Id. 46.

global administrative bodies, but whose interests are disregarded by those bodies.\textsuperscript{4} The following principles have emerged in GAL, seeking to overcome the problem of the disregarded: procedural participation and transparency; reasoned decisions; and review.\textsuperscript{5} Of these, Stewart argues that legally binding review is a true accountability mechanism, being a mechanism that protects “organizational ‘outsiders’ by influencing ‘inside’ decision makers to give regard to their interests”.\textsuperscript{6} Transparency, non-decisional participation, reason-giving, and non-binding review are “responsiveness-promoting measures” which provide incentives to global administrative bodies to consider otherwise disregarded interests, but are not accountability mechanisms.\textsuperscript{7}

This paper first considers the governance regimes of the IFC Performance Standards and the Equator Principles in light of GAL theory, considering the influence of different institutions and actors, especially NGOs. There are a variety of NGOs with different agendas, but this paper generally refers to NGOs without making distinctions and is primarily concerned with social justice NGOs that advocate for project-affected people. The IFC Performance Standards and Equator Principles were both established to maintain legitimacy in the face of NGO pressure, and to improve the sustainability of investments by upholding the interests of people affected by investments, among other things. Private financial institutions established the Equator Principles, incorporating the normative standards of the IFC’s Performance Standards. However, Equator Principles Financial Institutions (EPFIs) have chosen to have a weak governance regime that does little to promote EPFI responsiveness to project-affected people because of EPFIs’ shared interest in avoiding review and enforcement. By contrast, the IFC and its Compliance Advisor/Ombudsman (CAO) review body administer the IFC Performance Standards in a relatively robust regime that encourages the IFC to be responsive to the interests of people affected by IFC-supported projects through complaints predominantly brought by NGOs. In addition, through periodic reviews of the Performance Standards, the IFC, CAO and NGOs participate in agenda-setting and negotiation for the Performance Standards, which in turn influence the Equator Principles.

The paper then looks at the palm oil industry, the RSPO, and the IFC, considering the two case studies of the Wilmar Group and Dinant. Politics amongst RSPO members has led to transparency and review measures, advocated for by reputation-sensitive non-producer members keen to promote compliance amongst RSPO producer members to avoid free-riding and maintain the RSPO’s legitimacy. The Wilmar case study shows how the activities of the CAO and NGOs in the governance regime for the IFC promote responsiveness to people affected by IFC-supported projects. The Wilmar case prompted a review by the World Bank Group of its palm oil industry involvement, which allowed the CAO and NGOs to participate in decision-making on the IFC’s involvement in the

\textsuperscript{4} Stewart, supra note 3, pp. 5-14.
\textsuperscript{5} Kingsbury et al, supra note 3, pp. 37-40.
\textsuperscript{6} Stewart, supra note 3, p. 8.
\textsuperscript{7} Id.
industry and role at the RSPO. In addition, the Wilmar case gave rise to dialogue between the CAO and IFC, influenced by NGOs, about interpretation and implementation of the Performance Standards. By contrast, the RSPO’s weak response to complaints regarding Wilmar due to politics amongst members reluctant for the RSPO to “police” or judge members undermined the RSPO’s legitimacy. The Wilmar case also highlights EPFIs’ lack of transparency. Yet, despite the World Bank Group’s robust response to the Wilmar case, the Dinant case casts doubt on substantive improvements to IFC behavior from CAO reviews.

The IFC’s adoption of GAL and EPFIs’ resistance to GAL can be explained, but not justified, by the IFC’s being a public international organization, and EPFIs being private financial institutions. However, EPFIs cannot legitimately claim to uphold the Equator Principles that promote the interests of project-affected people while resisting measures that promote responsiveness to project-affected people. The IFC promulgates sustainability standards through increasing EPFI membership, which means that it has an interest in promoting GAL for legitimacy in its promulgation of sustainability standards aimed at upholding the interests of project-affected people.

2. The Governance Regimes of the IFC and the Equator Principles

2.1. The IFC, its Performance Standards, and its Governance Regime

The IFC was established in 1956 to finance private industry in countries borrowing from the World Bank. There are 184 IFC member countries, which have voting power based largely on their shareholding. Members appoint the Board of Governors, which delegates power to the Board of Directors. In the 2013 financial year, the IFC invested USD 18.3 billion in 612 projects.

The IFC positions itself as a leader in sustainable development as a means of maintaining its legitimacy in the face of criticism. The IFC introduced environmental and social “Safeguard Policies” in 1998, following civil society pressure led by NGOs concerning the Pangue Dam in Chile. These Safeguard

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10 Articles of Agreement (as amended through 27 June 2012), Art IV, IFC, available at <www1.ifc.org/wps/wcm/connect/1c95b500484cb68d9f3dbf5f4fc3f18b/IFC_Articles_of_Agreement.pdf?MOD=AJPERES>
11 Id.
Policies were replaced by the Performance Standards in 2006. The Performance Standards set out criteria for IFC clients, addressing social and environmental issues, covering areas such as labor conditions, pollution, biodiversity, and indigenous peoples. The IFC’s obligations are set out in its Policy on Environmental and Social Sustainability (Sustainability Policy), which requires that the IFC not finance an investment activity unless it is expected to meet the Performance Standards. The most recent edition of the Performance Standards came into effect on 1 January 2012.

Performance Standard 1 contains measures reflecting GAL principles of transparency, participation, and review, which encourage clients to respond to the interests of project-affected people. Performance Standard 1 provides for the assessment and management of environmental and social risks and impacts, including requiring that clients disclose project information to and consult with potentially adversely affected communities. Clients are to provide a grievance mechanism for project-affected people where appropriate.

The Sustainability Policy sets out the IFC’s obligations to govern its clients through due diligence, monitoring and enforcement of environmental and social standards. The IFC classifies projects within defined categories based on the level of severity of potential adverse impacts, which determines the scope of IFC assessment procedures applicable to a project. In cases of non-compliance, the IFC is to work with its client to bring it into compliance, but can exercise the

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19 IFC’s 2012 Policy on Sustainability, supra note 15. The 2006 Policy on Sustainability is drafted in different terms, but imposed similar obligations (2006 Policy on Sustainability, supra note 16).

20 IFC’s 2012 Policy on Sustainability, supra note 15, 8.

IFC’s contractual rights and remedies if necessary. 22

The IFC’s Sustainability Policy and Access to Information Policy apply the principles of transparency and review to the IFC itself, promoting its responsiveness to project-affected people. The Access to Information Policy sets out detailed provisions on what information the IFC should disclose and how access is to be provided for institutional information about the IFC and project-level information on investments and advisory services. 23 The Sustainability Policy provides for the CAO as an independent oversight authority for the IFC. 24

The IFC is subject to a high level of responsiveness-promoting measures because as a “public” entity, 25 being an international organization with states as members, it is more sensitive to demands for governance to maintain its legitimacy. Some of the most influential World Bank member states — the United States and European States such as the United Kingdom, Switzerland, Netherlands, and Germany — champion accountability mechanisms in the World Bank Group, 26 including the IFC. 27 The IFC’s CAO was established in 1999 in response to civil society pressure about — and the outcome of an investigation into — the Pangue project, 28 and pressure from the IFC’s Board of Directors. 29 The IFC’s sustainability governance structure, including its Sustainability Policy, Access to Information Policy and CAO all serve to protect its legitimacy as a public institution engaged in funding development.

2.1.1. CAO

The CAO’s independence as the IFC complaints mechanism 30 is important for its legitimacy. The CAO is independent from IFC management in that the CAO is

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29 Bissell and Nanwani, supra note 27, 15.
30 Although the CAO provides governance for the Multilateral Investment Guarantee Agency as well as the IFC, this paper refers only to the IFC for ease of reference because the IFC is the focus of this paper (although many of the observations may be relevant to MIGA).
appointed by, and reports to, the President of the World Bank Group. In addition, the CAO recruits Office of the CAO staff, and CAO professional staff contracts prevent professional staff from employment at the IFC for two years after they cease to work for the CAO.

The CAO aims to resolve complaints regarding IFC projects from project-affected people, promoting the IFC’s responsiveness to the interests of project-affected people. The CAO has three roles: Ombudsman, Compliance, and Advisor. The CAO Ombudsman assesses eligible complaints and determines whether a collaborative resolution is possible or the complaint should be referred to CAO Compliance. If referred, CAO Compliance determines whether the complaint merits an audit, and if so conducts and reports on an audit assessing IFC compliance with the IFC Performance Standards, among other things. If the IFC is not in compliance, the CAO monitors the case until the IFC is in compliance.

2.1.2. NGOs

The high rate of NGOs as signatories to complaints suggests that NGOs have a crucial monitoring and enforcement role in the IFC Performance Standards RSS scheme. Complaints to the CAO can be made by multiple groups or anonymously, so it is difficult to assess how many, if any, were made by community members without NGO involvement. Nonetheless, the high level of NGO involvement is illustrated by statistics from the CAO that:

- In the 2012 financial year, the proportion of complaints signed by:
  - Community members was 27 per cent;
  - International NGOs was 39 per cent;
  - National NGOs was 45 per cent; and
  - Local NGOs was 55 per cent.

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31 About IFC: Organization, supra note 9.
33 Id. 7.
35 CAO Operational Guidelines, supra note 32, 16.
36 Id. 21-25.
37 Id. 26.
39 Even if all of the claims that had community members as signatories were not signed by any NGO, that would mean that at least 73 per cent of complaints in FY 2012 and at least 76 per cent of complaints in FY2011-2010 were signed by at least one NGO.
40 CAO 2012 Annual Report, 6, CAO, available at <www.cao-ombudsman.org/publications/documents/CAOAualReport2012.pdf> (The CAO’s report refers to civil society organizations, but provides no definition, so the term “NGO” was used instead in this paper for consistency with the terms of the rest of the paper).
• From the 2000 to 2010 financial years, the proportion of complaints signed by:
  o Community members was 24 per cent;
  o International NGOs was 14 per cent;
  o National NGOs was 18 per cent; and
  o Local NGOs was 43 per cent.\textsuperscript{41}

The statistics show that the complaints mechanism is most frequently used by NGOs, rather than individuals. This may indicate that the CAO process is difficult to access for project-affected people who are not “organized” (in the sense of forming an organization). It may also indicate that the CAO complaints mechanism encourages the formation of organizations — the high number of local NGO signatories may be the result of organizations being formed by project-affected people in order to navigate the CAO complaints procedure.\textsuperscript{42}

The key role of NGOs in the IFC governance regime raises issues about the operation of the regime. The CAO complaints mechanism exists to allow people affected by IFC-supported projects to have their concerns addressed, but most claims are brought by NGOs. Local NGOs are the largest proportion of signatories, and many of the local NGO signatories may be NGOs established solely by projected-affected people. In any case, the CAO states that community members are involved in all complaints,\textsuperscript{43} and the CAO screens complaints to ensure that they are made by or on behalf of project-affected people.\textsuperscript{44} So the CAO’s complaints assessment process tries to address the risk that NGOs do not represent the interests of project-affected people, which should protect the CAO complaints process from being coopted by interests other than those of project-affected people.\textsuperscript{45} Nonetheless, there is a concern that individuals find the complaints process difficult, and the IFC’s responsiveness to project-affected people through the CAO depends on NGO intervention.

2.2. \textit{Equator Principles Regime}

EPFIs claim to follow sustainability standards based on the IFC Performance Standards. The 2006 Equator Principles II required that the IFC Performance Standards be applied to projects in non-OECD countries or OECD countries not designated as “High-Income under the World Bank Development Indicators Database”.\textsuperscript{46} Equator Principles III came into effect on 4 June 2013, although

\textsuperscript{43} \textit{CAO 2012 Annual Report}, supra note 40, 6.
\textsuperscript{44} \textit{CAO Operational Guidelines}, supra note 32, 15.
\textsuperscript{45} Many NGOs are aware of their potential legitimacy issues, and are taking steps to promote their own accountability to their stakeholders: Bissell and Nanwani, \textit{supra} note 27, pp. 54-55.
Equator Principles II can be applied to new transactions until 31 December 2013.\textsuperscript{47} Equator Principles III require that the Performance Standards be applied in countries that are not deemed to have robust environmental and social governance, as listed on the Equator Principles website.\textsuperscript{48} EPFIs undertake to provide project finance to projects with total project capital costs of USD 10 million or more only if the project conforms to the Principles.\textsuperscript{49} Under Equator Principles III, EPFIs also undertake not to provide project-related corporate loans of USD 50 million or more where the total aggregate loan amount is at least USD 100 million unless the project conforms with the Principles.\textsuperscript{50}

Commercial banks established the Equator Principles to maintain their reputations in the face of NGO-led campaigns, making use of the IFC’s legitimacy in sustainable development. Commercial banks became targets for NGO campaigns in the 1990s as the project finance market expanded and there was increased public awareness of the level of decision making by commercial banks regarding environmental and social risk management.\textsuperscript{51} Following high profile NGO-led campaigns,\textsuperscript{52} some leading commercial banks met with the IFC in October 2002.\textsuperscript{53} A subsequent process of drafting and consultation between banks, the IFC and NGOs produced the Equator Principles, which were launched in June 2003 by 10 commercial banks at IFC headquarters.\textsuperscript{54}

The cursory reporting requirements of Equator Principles II meant that their implementation was difficult to monitor,\textsuperscript{55} but Equator Principles III contain significantly improved transparency provisions in response to NGOs and the strategic review of the Equator Principles. Equator Principles II merely required annual reporting by EPFIs of the number and category of projects to which they applied the Principles.\textsuperscript{56} The draft 2013 Equator Principles proposed increased reporting and transparency as recommended by Environmental Resources


\textsuperscript{49} Equator Principles II, supra note 46, Scope and Statement of Principles.

\textsuperscript{50} Equator Principles III, supra note 48, Scope.


\textsuperscript{52} Id.

\textsuperscript{53} Id. 60.

\textsuperscript{54} Id.


Management in its 2011 strategic review of the Equator Principles, and the reporting provisions were further expanded in response to NGOs during the consultation process. The 2013 Principles’ reporting requirements include reporting project-specific data, subject to the client’s consent, after a project’s financial transactions reach financial close, which is when all conditions precedent to initial drawing of the debt have been satisfied or waived. EPFIs must now disaggregate finance and loan data according to sector, region, country designation, and whether an independent review has been carried out. In addition, EPFIs are now required to report on implementation of the Principles in their organizational structures and decision-making.

EPFIs have refused calls to establish a review mechanism for EPFI compliance, and sanctions for EPFI non-compliance are limited. Equator Principles II did require that borrowers establish a grievance mechanism and that an independent expert review a project’s compliance with the Equator Principles. These measures promote the responsiveness of borrowers — but not EPFIs — towards the interests of project-affected people. Most recently, the Equator Principles Association rejected a recommendation for Equator Principles III to establish an official grievance mechanism as “not appropriate” in light of the voluntary nature of the Principles. Equator Principles Governance Rules were established in 2010, providing for a delisting process for institutions that fail to pay their annual fee or to comply with reporting requirements. However, there is no provision for delisting non-compliant institutions more broadly, so an EPFI could consistently fail to apply the IFC Performance Standards to projects in breach of the Equator Principles and yet there would be no basis on which to delist that institution.

EPFIs have therefore taken the view that because the Equator Principles are not

60 Equator Principles III, supra note 48, 14 and 17.
61 Id. 13.
62 Id. 14.
64 Equator Principles, supra note 46, Principles 6 and 7.
mandatory, but are instead private self-regulation by financial institutions, the governance of EPFIs’ compliance with the Principles should be weak and not subject to oversight from a review body. EPFIs have thus used the voluntary nature of the Equator Principles to justify treating the Principles as non-binding. This view has outweighed any concern about protecting the integrity of the Equator Principles RSS scheme from the risk of free riding EPFIs.

Absent better governance for EPFIs, there are two main incentives for EPFIs to comply with the Equator Principles and be responsive to project-affected people: firstly, minimization of costs, and secondly, protection of reputation. The first incentive is not a matter of governance, rather a business strategy of minimizing the risks of a project to protect a bank’s investment. The second incentive has emerged as an important feature of voluntary governance regimes such as the Equator Principles, and has been referred to as an “alternative accountability mechanism” in GAL literature and a responsiveness-promoting measure by Stewart. NGOs encourage compliance by monitoring the activities of EPFIs and mounting public campaigns to shame non-complying EPFIs into compliance.

However, the lack of transparency has meant it has been difficult to monitor EPFIs’ activities; hence reputation has been a weak measure for encouraging compliance because EPFIs could realistically expect to suffer little or no reputational damage for harm to the interests of people affected by EPFI-financed projects. There is evidence that the Equator Principles are reflected in EPFIs’ organizational structures and decision-making processes, but this does not constitute evidence of responsiveness to the interests of project-affected people as such.

2.3. Review Processes — Standard-Setting by Negotiation

Periodic reviews of the IFC Performance Standards involve the CAO, NGOs and EPFIs in negotiation of standards that affect the Equator Principles.

The CAO engages in standard-setting for the IFC Performance Standards in two ways: compliance decisions that interpret the IFC Performance Standards (discussed below with reference to palm oil), and participation in reviews of the Performance Standards. The CAO played a key role in the process that led to the 2006 Performance Standards, beginning with its review of the Safeguard Policies in 2003, and commenting on the IFC’s response. In the review of the 2006

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68 Id. 213-214.
69 Kingsbury et al, supra note 3, 57.
70 Stewart, supra note 3, 33.
71 Hardenbrook, supra note 67, 213-214.
72 Meyerstein, Transnational Private Financial Regulation, supra note 55, 553-556.
Performance Standards and associated policies, the CAO released an advisory note in 2010 setting out its views on reforms following consultation with civil society.\(^4\) This consultation included civil society outreach by the CAO in relation to the IFC’s Policy on Disclosure of Information, and a study of the perceptions of local stakeholders for selected IFC-supported projects on the implementation of the Performance Standards.\(^5\) The IFC released a document setting out its response to the CAO’s recommendations on 1 June 2010,\(^6\) demonstrating that the CAO’s involvement in the review process prompts the IFC to give reasons for drafting decisions about new versions of the Performance Standards.

Two examples suggest that the 2012 Performance Standards were influenced by the CAO’s recommendations. The CAO commented that the Performance Standards be updated in accordance with the Protect, Respect, Remedy Framework developed by the UN Special Representative on Business and Human Rights.\(^7\) The 2012 Performance Standards refer to the Framework, including the responsibility of business to respect human rights, although the Standards do not reflect the Framework’s principle of comprehensive human rights due diligence.\(^8\) The CAO also recommended that the Performance Standards address issues for migrant workers, and 2012 Performance Standard 2 now does so.\(^9\)

NGOs also contributed to the review that produced the 2012 Performance Standards. A joint “Submission by Civil Society Organizations to the International Finance Corporation” was submitted on 11 March 2010, signed by 92 civil society organizations. By way of example, a key recommendation was the inclusion of “free, prior and informed consent” (FPIC) as a requirement for projects affecting indigenous communities.\(^10\) 2012 Performance Standard 7 introduced requirements that clients obtain indigenous peoples’ FPIC when a project involves “the relocation of Indigenous Peoples from communally held


\(^6\) IFC’s Response to CAO Advisory Note (June 1, 2010), CAO, available at www.cao-ombudsman.org/howwework/advisor/documents/IFCResponseCAOAdvisoryNote_June2010.pdf.

\(^7\) Advisory Note, supra note 74, 8.

\(^8\) 2012 IFC Performance Standards, supra note 14, Performance Standard 1, page 1;


lands and natural resources subject to traditional ownership or under customary use.”81 2012 Performance Standard 7 also requires FPIC where a project may “significantly impact on critical cultural heritage” or use cultural heritage.82 In addition, the Equator Principles Association had input into the most recent Performance Standards review.83 The IFC had a consultation meeting with the Equator Principles Steering Committee84 and the Equator Principles Association made a submission.85 Thus, the relationship between EPFIs and the IFC is not unidirectional.86 In the other direction, revisions to the IFC Performance Standards prompt revisions to the Equator Principles. Thus, the CAO, EPFIs, and NGOs/civil society (directly and through the CAO) participate in the negotiation of the IFC’s Performance Standards RSS scheme, which indirectly sets standards for the Equator Principles.87

3. Financing the Palm Oil Sector

The analysis above considered the Performance Standards and Equator Principles RSS schemes, and the influence of different actors on the schemes’ operation and negotiation of standards. This part of the paper discusses the Roundtable on Sustainable Palm Oil (RSPO) as a third RSS scheme, two case studies of IFC palm oil investments, and the involvement of the CAO, RSPO, and EPFIs. The case studies show: how interactions between NGOs, the CAO, and the IFC promote IFC responsiveness to project-affected people; the relatively weak RSPO response to complaints; the broader standard-setting roles of the CAO and NGOs through enforcement; and the lack of EPFI transparency.

3.1. Palm Oil and the RSPO

The palm oil sector is growing and is associated with environmental and social harms, so the RSPO was established to prevent such harms and maintain the industry’s legitimacy.

The World Bank Group has identified various benefits from palm oil to justify

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81 2012 IFC Performance Standards, supra note 14, Performance Standard 7, 4-5.
82 Id.
83 Meyerstein, Transnational Private Financial Regulation, supra note 55, 573-574.
86 Hardenbrook, supra note 67, 230-231.
its ongoing engagement with the sector. Palm oil is extracted from oil palm fruit through milling, refining and extraction processes, and is used in cooking oil, processed food, cosmetics, detergent and other products. Demand for palm oil has increased at a high rate in recent decades, from 3.8 million tonnes in 1980 to 36.2 million tonnes in 2009. The World Bank Group sees palm oil as useful for addressing food security issues from global population increases, and for poverty reduction given income export earnings, employment and income generation, and the relatively cheap price of palm oil as a food. Palm oil can be used as a biofuel, and it was for biofuel production that Malaysia and Indonesia (the largest producers of palm oil) pursued aggressive palm oil production policies, although the World Bank Group found that oil palm is not widely grown as a biofuel.

However, there are significant environmental and social risks associated with oil palm plantations. Oil palm plantations are associated with deforestation and decreased biodiversity. The palm oil industry can increase greenhouse gas emissions from land clearing, draining of peatlands and methane released from effluent treatment ponds. In addition, oil palm plantation development is associated with land rights disputes, disruption of local communities’ culture, loss of locals’ livelihoods, and poor working conditions. The encouragement of large-scale oil palm projects by the World Bank Group has been criticized as inherently susceptible to these risks.

The multi-stakeholder RSPO RSS Scheme was established to address criticism of the industry. The RSPO was formally established on 8 April 2004 under the Swiss Civil Code, following a mobilization and negotiation process commenced by the World Wildlife Fund (WWF) in 2001. RSPO member categories include oil palm growers, palm oil processors and traders, consumer goods manufacturers, NGOs, banks and investors, and retailers. The RSPO Executive Board members

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90 Id. 15.
91 Id. 14-15.
92 Id. 13.
94 Framework and Strategy, supra note 89, 16.
95 Id. 17.
96 Id.
97 Id. 21.
99 Framework and Strategy, supra note 89, 32.
represent these different categories. Of the RSPO’s 11 bank or investor members, seven are EPFIs and one is the IFC.\textsuperscript{102} The RSPO has established international certification schemes for sustainable palm oil production and supply chains. Palm oil is RSPO Certified as sustainably produced if certified by an approved certification body as meeting the standards set out in the RSPO Principles and Criteria for Sustainable Palm Oil Production.\textsuperscript{103} The Principles and Criteria concern: transparency, compliance with applicable laws, economic and financial viability, best practices by growers and millers, environmental responsibility and conservation, employees, and individuals and communities affected by growers and mills.\textsuperscript{104} Supply chains for certified sustainable palm oil are subject to supply chain certification in order for a certification logo to be used on the end product.

3.2. \textit{RSPO Governance}

NGO, retail, financier, and consumer goods manufacturer RSPO members have successfully advocated for a RSPO code of conduct and grievance procedure in order to protect their reputations by defending the RSPO’s legitimacy and their involvement in the RSPO. However, the grievance procedure lacks the independence of the CAO.

Incidents in 2005 and 2006, including NGO campaigns, put pressure on the RSPO and raised questions about the RSPO’s role. Friends of the Earth ran a campaign with the “Ape Alliance” launched in September 2005,\textsuperscript{105} linking deforestation for oil palm cultivation to destruction of orangutan habitat on Borneo.\textsuperscript{106} In September 2005, haze caused by open burning in Indonesia, including on oil palm plantations, affected Malaysia.\textsuperscript{107} Labor organizations lobbied the RSPO in 2005 and 2006 to address a labor dispute concerning a Musim Mas plantation in Indonesia, in which 701 employees were dismissed and their families evicted from plantation estate housing.\textsuperscript{108} The Musim Mas crisis in

\begin{thebibliography}{9}
\bibitem{105} The Future’s not Bright if You’re Orange (Sept. 1, 2005), Friends of the Earth, <www.foe.co.uk/news/orangutan_report.html>.
\end{thebibliography}
particular highlighted confusion about the RSPO’s role and mandate, and how it should respond to allegations of misconduct.

These crises prompted NGOs, consumer goods manufacturers, financiers, and retailers at Executive Board meetings to advocate improved governance, driven by concerns of legitimacy and reputation. Cadbury Schweppes and the Body Shop advocated for transparency amongst RSPO members in response to the Musim Mas case. HSBC argued for a Code of Conduct to encompass agreement on how the RSPO addresses issues such as the recent haze. Unilever and the Body Shop took leading roles on initial Code of Conduct drafts. WWF emphasized the implications of the Musim Mas case for the RSPO’s reputation and RSPO NGO members. Cadbury Schweppes argued that such cases also challenge the reputations of businesses, and that the RSPO must respond.

Producers in the RSPO were resistant to proposals of RSPO review of members. The Malaysian producers representative raised a concern that RSPO intervention would undermine national sovereignty in terms of the primacy of national law and courts. Following resolution of the Musim Mas case, the Indonesian producers representative observed that European campaign pressures were transferred through the RSPO to Musim Mas, and the Malaysian produces representative advocated that the RSPO should hold “a moderate position whereby members under attack should be responsible for finding solutions.”

The RSPO established a Code of Conduct for members by the end of 2006, and procedures for complaints alleging breaches of the Principles and Criteria for Sustainable Palm Oil Production, certification system, or the Code of Conduct, although the complaints process ultimately lacks independence. The Code of Conduct made annual RSPO member reporting compulsory, and WWF has sought to promote compliance by successfully advocating that the Secretariat monitor...
The grievance procedures have developed over time — initially the RSPO established an arbitration panel, the terms of reference for which were expanded to address grievances in mid-2006, and a further panel was established to consider RSPO membership issues in early 2007. The Principles & Criteria included complaints procedure provisions from its establishment. These complaints bodies have become the Complaints Panel, which comprises five members: four from the Executive Board and one independent of the Board. The Complaints Panel proposes sanctions to the Executive Board if a complaint is not resolved satisfactorily, but does not itself impose sanctions.

The RSPO’s variety of membership results in its willingness to adopt reporting and review mechanisms — unlike the EPFIs that have a common interest in avoiding review of their activities and maintaining confidentiality — but also the weak nature of these mechanisms. The RSPO states that its complaints procedures serve to protect its integrity, linking review mechanisms to the RSPO’s legitimacy, which in turn protects members’ reputations. Since discussion of the establishment of a grievance panel began, it was rightly anticipated that most complaints would involve oil palm plantations. As set out above, NGOs, consumer goods manufacturers, financiers and retailers were most concerned about reputational damage from unsustainable practices at oil palm plantations undermining the legitimacy of the RSPO, yet these groups were not in control of the plantations. Accordingly, these reputation-sensitive groups advocated transparency and review measures to promote compliance amongst growers, and had little to lose from such measures because as non-producers they were unlikely to be subject to a damaging review process. If the RSPO only contained producers, it would likely have mirrored EFPIs’ resistance to review. Instead, the Executive Board established processes for a Complaints Panel that is not an independent review body, but includes a majority of members from the Executive Board, and can only make recommendations to the Executive Board, which has the ultimate decision-making power for complaints.

3.3. **Wilmar Group’s Palm Oil Business and the CAO**

In this context of the palm oil industry and RSPO, the Wilmar complaint to the CAO sparked a World Bank Group review of engagement with the industry, and

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119 *Id.* 1.3.
illustrates the strengths of the IFC’s RSS scheme.

From 2003 to 2008, the IFC made four palm oil investments in the Wilmar Group, comprising Wilmar International Limited and its subsidiaries. Wilmar Group is a Singapore-based agribusiness with operations in many countries including Indonesia, Malaysia, China and the Ukraine. The Wilmar Group has a diverse business including oil palm cultivation, palm oil refining, sugar milling and refining, oleochemicals, and fertilizers manufacturing. None of the IFC’s investments were for the exploitation of any particular oil palm plantations, but the Summary of Proposed Investment for each project referred to the Group’s ownership of plantations. One of the projects approved was a palm oil refinery in the Ukraine, and another was an investment in a trade facility to “ensure the continuous operation of the [crude palm oil] supply chain and the preservation of all economic interests and employment associated with that chain such as plantation, transportation, storage, processing and shipping.”

In July 2007, several NGOs and Kalimantan communities filed a complaint with the CAO regarding Wilmar’s actions in West Kalimantan and the IFC’s Wilmar investments. The CAO complaint was part of a three-part strategy, in which a complaint was also made to the RSPO, and NGOs lobbied Wilmar’s palm oil buyers and financiers. The CAO complaint criticized the IFC’s supply chain assessment for the investments, arguing that the IFC’s classification of two projects in particular had meant that the IFC avoided properly assessing the negative consequences from oil palm plantations. The complaint also made allegations of failures to meet the 2006 Performance Standards, including: taking over customary lands of indigenous peoples without due process, failure to negotiate with communities or comply with agreements, and failure to carry out or wait for government approval of environmental impact assessments.

CAO Compliance determined that an audit of issues referred by the Ombudsman was


123 Id.


125 Audit Report, supra note 121, 22-23.

126 Id. 24-25.


129 Id.
merited.\textsuperscript{130}

The CAO Audit Report dated 19 June 2009 found that the IFC was not in compliance.\textsuperscript{131} In the CAO’s view, “Because commercial pressures dominated IFC’s assessment process, the result was that environmental and social due diligence reviews did not occur as required.”\textsuperscript{132} The CAO found that the IFC took a narrow view of the supply chain consequences of each project, which was inconsistent with the IFC’s “asserted role, mandate of reducing poverty and improving lives, and a commitment to sustainable development”.\textsuperscript{133}

The CAO’s findings prompted a suspension of World Bank Group financing of palm oil projects pending the development of a comprehensive strategy for palm oil investments.\textsuperscript{134} The IFC’s response to the compliance audit acknowledged “weakness” in its Environmental and Social Review Procedures and that supply chain performance should have been more closely scrutinized, stating it was developing a comprehensive strategy for palm oil investments.\textsuperscript{135} The World Bank President instructed the World Bank Group in September and October 2009 to suspend investments in the palm oil sector until the strategy was developed.\textsuperscript{136} At a project level, the CAO’s findings caused the IFC to review Wilmar’s oil palm plantation operations against the Performance Standards and to undertake to improve its engagement with civil society groups, both of which the CAO monitored.\textsuperscript{137}

The CAO took the opportunity to comment on RSPO standards compared to IFC standards, effectively asserting the primacy of the latter, which suggests that the CAO views the RSPO as a potential competitor in sustainability standard setting. The CAO observed that Wilmar’s stated support of the RSPO did not supersede the need to apply IFC policies, procedures, and standards, and that the RSPO Principles and Criteria did not address all of the issues safeguarded by the IFC Performance Standards,\textsuperscript{138} so RSPO certification is not sufficient for

\begin{footnotesize}
\begin{enumerate}
\item \textsuperscript{130} \textit{Audit Report, supra} note 121.
\item \textsuperscript{131} \textit{Id.} 2-3.
\item \textsuperscript{132} \textit{Id.}
\item \textsuperscript{133} \textit{Id.}
\item \textsuperscript{136} Indonesia/Wilmar Group-01/West Kalimantan, CAO, supra note 134.
\item \textsuperscript{138} \textit{Audit Report, supra} note 121, 24.
\end{enumerate}
\end{footnotesize}
Performance Standards compliance. Wilmar was an RSPO member at the time of the events that were the subject of the complaint, but not RSPO certified for palm oil production since production certification was established in 2007.\(^{139}\)

In addition, the CAO encouraged the IFC to undertake standard-setting in the palm oil sector through the RSPO. Under the action plan agreed with the CAO following the Wilmar case, the IFC undertook to strengthen the RSPO including through “Direct support of RSPO’s Biodiversity Technical Committee, support of pilot projects through IFC’s Biodiversity and Agricultural Commodities Program (BACP), IFC staff involvement in RSPO working groups, requirements for client adherence to RSPO Principles and Criteria”.\(^{140}\) Given the CAO’s influence on the IFC, increased IFC participation in the RSPO increases the CAO’s indirect influence on the RSPO.

3.4. **RSPO and Wilmar**

The RSPO is less transparent and rigorous than the CAO about the Wilmar complaint — the RSPO contented itself with Wilmar’s undertakings to improve sustainability performance, and adopted a cooperative attitude towards the CAO. The RSPO does not provide information regarding the 2008 complaint concerning Wilmar on its complaints page, making its complaints process opaque for that period. The RSPO Executive Board minutes reveal that RSPO merely spoke with the parties, sought access to CAO documents, and accepted Wilmar’s undertakings to improve its sustainability practices.\(^{141}\) However, it appears that the RSPO did not rigorously monitor Wilmar’s adherence to its undertakings given the complaints below.\(^{142}\)

The RSPO grievance mechanism would benefit from greater independence, like the CAO, so that it could more robustly review members. The RSPO grievance mechanism was relatively new and controversial within the RSPO at the time, which may explain why it took a relatively passive role while the CAO made formal determinations. Predictably, the RSPO’s lack of formal sanction of Wilmar and Wilmar’s subsequent poor practices gave rise to accusations that RSPO was merely an exercise in ‘green washing’.\(^{143}\)

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\(^{140}\) *Framework and Strategy*, supra note 89, 71.


\(^{143}\) *Id.; Accountability Counsel and the Center for International Environmental Law letter to World Bank Group Palm Oil Review dated August 31, 2010*, 6, available at
3.5. Further Complaints to the CAO and the RSPO

Further complaints regarding Wilmar indicate ongoing poor social sustainability practices, and one complaint made to both bodies resulted in the RSPO deferring to the CAO.

Two further complaints were filed at the CAO regarding Wilmar’s actions in Indonesia, including allegations that Wilmar failed to obtain community consent for land clearing. The second complaint, filed on 1 December 2008, concerned Wilmar’s activities in Sumatra, specifically in Jambi and Riau. The Riau dispute was resolved by agreement following mediation, but the Jambi complaint was not, and was filed as a third complaint to the CAO on 9 November 2011. Based on agreement between the parties, mediation of this third complaint commenced in March 2012 conducted by a team of CAO members and local government staff. The mediation is ongoing, and there are current discussions about how to proceed following Wilmar’s sale of its interest in Asiatic Persada (the subject of the third complaint) in April 2013 to non-RSPO member and non-IFC funded companies.

The RSPO appears to have deferred to the CAO in relation to this third complaint. A complaint was made to the RSPO on 14 February 2011 regarding Asiatic Persada. The RSPO website states that the CAO offered mediation services and the RSPO is awaiting an update. The primary aim of both complaints mechanisms is to resolve the concerns of project-affected communities. Accordingly, it makes sense that the RSPO accepted the CAO’s offer of mediation services rather than establishing multiple dispute resolution fora, although the RSPO’s reluctance to make formal findings of noncompliance against members was probably a motivating factor.

There have also been three further complaints to the RSPO since July 2012 against Wilmar Group companies — two in Indonesia and one in Nigeria — in
which the CAO has not been involved. The complaints include allegations of inadequate disclosure and consultation with local stakeholders, illegal land acquisition, and other breaches of RSPO standards.

3.6. **EPFIs and Wilmar**

EPFI confidentiality makes it hard to determine whether EPFIs finance Wilmar oil palm projects, but it appears that some EPFIs invest in, and provide loans to, Wilmar. Friends of the Earth commissioned a report by Profundo on Wilmar’s financiers, and found that Barclays, BNP Paribas, Citigroup, Credit Agricole, Deutsche Bank, HSBC, ING, KBC Group and Rabobank provide bank loans to Wilmar. All of these banks are EPFIs except for Deutsche Bank, which used to be one. Interestingly, Deutsche Bank fund management company DWS disposed of Wilmar International stock in early 2011, when Deutsche Bank appears to have been an EPFI. Facing Finance also has data that BNP Paribas, ING and KBC Group provide loans to Wilmar International. Neither Friends of the Earth nor Facing Finance indicate whether these banks provide project finance for Wilmar’s palm oil operations. However, Facing Finance does indicate that BNP Paribas, ING, KBC Group and UniCredit Group are indirect investors in Wilmar’s Indonesian palm oil operations.

Consideration of the Wilmar case demonstrates how the lack of transparency requirements under the Equator Principles makes it difficult to monitor EPFIs. None of the information publicly available about EPFI financing of Wilmar

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158 Id.
demonstrates breaches of the Equator Principles. Investment in a company, for example through share ownership, is not activity to which Equator Principles II applied. It is possible that these EPFIs did not provide project finance to Wilmar, or that any such project finance fell outside of the application of Equator Principles II. The key point is that it is not possible to monitor whether EPFIs have complied with the Equator Principles due to their lack of transparency.

3.7. Outcomes of the World Bank Group’s Palm Oil Sector Review

The World Bank Group reviewed its involvement in the palm oil sector in response to the first Wilmar complaint, producing the “World Bank Group’s Framework and IFC Strategy for Engagement in the Palm Oil Sector” (Framework and Strategy) in March 2011.159 The review process included “Nine multi-stakeholder consultations [which] reached over 2,500 stakeholders from 30 countries, and an interactive E-consultation, with participants from 51 countries.”160 The IFC strategy within the Framework and Strategy is based on the IFC’s being a relatively small provider of finance in the palm oil sector and includes:

(2) engaging selectively with key private sector partners throughout the industry’s supply chain […] who are able to demonstrate good management practices in environment and social sustainability and community and smallholder engagement; and (3) working with multi-stakeholder initiatives to develop voluntary industry-wide standards for sustainable development.161

Pursuant to the second point in the strategy, the IFC promotes the RSPO as an institution and standard-setter by requiring that IFC palm oil clients be RSPO members and encouraging certification.162 The last point in the strategy indicates the IFC’s intention to set standards in the palm oil industry, which is reflected in its involvement in the RSPO.163

The IFC’s work within the RSPO promotes smallholder participation, and is mandated by the Framework and Strategy. The RSPO defines smallholders as oil palm farmers “where the family provides the majority of labor and the farm provides the principal source of income, and where the planted area of oil palm is usually below 50 hectares in size.”164 The World Bank Group and RSPO recognize the risk of smallholders’ interests being disregarded by the RSPO RSS

159 Framework and Strategy, supra note 89.
160 Id. 5.
161 Id. 8.
163 Framework and Strategy, supra note 89, 32.
scheme because they may not have sufficient resources for certification. \(^{165}\) The IFC is a member of the Smallholders Working Group and Smallholder Funding Mechanism Workstream, \(^{166}\) and helped establish the RSPO Smallholder Support Fund announced in March 2013 to promote smallholder production of certified sustainable palm oil. \(^{167}\) The IFC’s work on smallholders is consistent with the third “pillar” of the Framework and Strategy, being “benefit sharing with smallholders and communities”, under which the World Bank Group is to support smallholder access to sustainable palm oil benefits through finance and advisory services. \(^{168}\)

The IFC might have undertaken these activities in the RSPO in any case, but the Wilmar case gave rise to opportunities for the CAO, NGOs and civil society to participate in the decision-making for the Framework and Strategy.

3.8. **Dinant’s Palm Oil Business**

The Dinant case study casts doubt on the IFC’s sustainability practices, despite the influence of the CAO in the Wilmar case.

The second case study concerns a CAO case that began in 2012 regarding the IFC’s financing of palm oil company Corporacion Dinant (Dinant) in Honduras, which has vertically integrated business in food and palm oil. \(^{169}\) A loan agreement between IFC and Dinant was concluded on 3 April 2009 to enable Dinant to develop young oil palm plantations, among other things. \(^{170}\) In June 2009, a military coup in Honduras overthrew President Zelaya and there were significant human rights violations by security forces. \(^{171}\) The government installed by the coup collaborated with wealthy landowners to violently suppress land rights claims. \(^{172}\) Dinant was allegedly linked to Miguel Facusse and the brutal crackdown on land rights protestors by Facusse’s private guards in the Aguan Valley where Facusse has extensive oil palm plantations. \(^{173}\) According to the


\(^{168}\) Framework and Strategy, supra note 89, 30-31.


\(^{170}\) Id. 5.


\(^{173}\) Id.
CAO, there are allegations of violence against land rights activists immediately preceding and following the coup.\textsuperscript{174} The first disbursement under the April 2009 loan agreement was executed on 15 November 2009.\textsuperscript{175} Dinant reported to the IFC in December 2009 that some of its Aguan Valley plantations had been invaded, prompting investigations by the IFC.\textsuperscript{176}

In early 2012, the CAO Vice President initiated an appraisal of the Dinant investment.\textsuperscript{177} Rights Action, an NGO, made allegations regarding Dinant in a letter to the World Bank Group President in November 2010,\textsuperscript{178} and the CAO Vice President decided to initiate the appraisal partly in response to that letter.\textsuperscript{179} The compliance appraisal concerned allegations that:

- Dinant “conducted, facilitated or supported forced evictions of farmers”,\textsuperscript{180}
- Violence “occurred because of inappropriate use of private and public security forces under Dinant’s control or influence”,\textsuperscript{181} and
- The IFC failed to promptly identify or respond to Dinant’s situation in light of the political and security issues following the coup in June 2009.

The Appraisal Report concluded that the Dinant investment merited a compliance audit.\textsuperscript{182}

Although the CAO does not refer to it, it is possible that the CAO Vice President was prompted to act in part by the decision of an EPFI to cancel a USD 20 million loan to Dinant.\textsuperscript{183} Deutsche Entwicklungsgesellschaft (DEG) is a German development bank that is part of the KFW Group, which is an EPFI. A campaign by FoodFirst Information and Action Network that presented a report to DEG on human rights violations associated with Dinant prompted DEG to investigate and decide to cancel its loan to Dinant on 8 April 2011.\textsuperscript{184} The lack of transparency for EPFIs means that it is unclear whether DEG viewed the Equator Principles as a reason to cancel the loan.

There is an ongoing campaign by a network of NGOs regarding the IFC’s financing of Dinant. Rights Action has continued its campaign, monitoring and

\textsuperscript{174} Appraisal Report, supra note 169, 7.
\textsuperscript{175} Id.
\textsuperscript{176} Id.
\textsuperscript{179} Appraisal Report, supra note 169, 1.
\textsuperscript{180} Id. 5.
\textsuperscript{181} Id.
\textsuperscript{182} Id.
\textsuperscript{183} Frank, supra note 172.
criticizing the CAO process for lack of transparency, which has been publicized by other NGOs such as Climate Connections and CorpWatch. In March 2013, a new campaign was launched by a group of NGOs including Friends of the Earth and Rights Action calling on the World Bank to cease support for Dinant. The NGOs allege ongoing human rights violations associated with Dinant, alleging 88 murders in the last three years and that two activists found in February 2013 were tortured and murdered, and that there has been a “state of impunity” around these murders.

3.9. Project-level Responsiveness

The cases of Wilmar and Dinant demonstrate how the CAO operates to improve the responsiveness of the IFC to project-affected people, but also the poor substantive outcomes that are possible despite the governance scheme.

Taken by itself, the Wilmar case can be viewed a success story for governance and accountability of the IFC. The transparency of the IFC and existence of the CAO enabled the first Wilmar complaint. The IFC’s reason giving by way of its response to the audit indicates that it took the findings seriously. Thus transparency, review and reason giving measures encouraged the IFC to be responsive to the interests of people affected by IFC palm oil investments. In addition, the World Bank Group suspension of palm oil investment suggests a suitably chastened group of international financial institutions seeking to avoid repetition of the adverse impacts from the Wilmar projects.

The RSPO response to complaints shows that transparency and review are not a panacea for project-affected people, particularly when an institution is unwilling to make adverse findings. The RSPO did not make formal findings or rigorously monitor Wilmar and this role was not fulfilled by the CAO because the IFC’s actions were the subject of CAO review, not Wilmar’s. The ongoing complaints and campaigns against Wilmar indicate that the company has not honored its undertakings to the RSPO.

In addition, the Dinant case raises serious questions about the efficacy of the CAO to encourage the IFC’s responsiveness to project-affected people. The agreement

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189 Id.

190 See, Saper, supra note 28, 1315-1316.
with Dinant was concluded in April 2009, prior to the CAO’s compliance audit report, so it is possible that those concluding the agreement were unaware of the serious findings of the report. Yet, the first disbursement to Dinant was made after the World Bank President had suspended palm oil investment. It is staggering that the IFC did not exercise greater caution in determining to execute the disbursement.

3.10. Enforcement as Standard-Setting

The Wilmar case demonstrates how the review process enables dialogue between the CAO and IFC regarding the Performance Standards, and promotes responsiveness to civil society. The CAO found that the IFC “did not meet the intent or the requirements of the Performance Standards”, which required that the IFC consider the supply chains of investments in its assessment of the category of investments.191 The CAO’s view of supply chain assessment reflects arguments in the complaint. As such, civil society’s views on interpretation of the IFC’s policies influenced the CAO’s findings and dialogue between the CAO and IFC.

The CAO’s interpretation of the Performance Standards applied their criteria for supply chain assessment to IFC project assessment. 2006 Performance Standard 1 provides for environmental and social risk assessment to take into account:

the role and capacity of third parties (such as local and national governments, contractors and suppliers), to the extent that they pose a risk to the project, recognizing that the client should address these risks and impacts commensurate to the client’s control and influence over the third party actions. The impacts associated with supply chains will be considered where the resource utilized by the project is ecologically sensitive, or in cases where low labor cost is a factor in the competitiveness of the item supplied.192

The CAO found that the palm oil sector has impacts on low cost labor and ecologically sensitive resources.193 Given the supply chain consequences, the CAO found that the IFC should not have categorized the projects such that the supply chain was excluded, and should have assessed suppliers and supply chains consistent with the Performance Standards.194

The IFC accepted the CAO’s interpretation of IFC project assessment obligations, but asserted the need for a nuanced standard for supply chain due diligence. The IFC accepted that the 2006 Performance Standards “included reference to the need to consider supply chains” and that it should have paid greater attention to the Ukraine refinery’s crude palm oil supply chain.195

However, the IFC also emphasized the varying level of control that clients will

191 Audit Report, supra note 121, 29.
192 2006 IFC Performance Standards, supra note 17, Performance Standard 1, 2.
193 Audit Report, supra note 121, 25.
194 Id. 27-30.
have over different parts of their supply chains. The IFC thus asserts the need for a nuanced, rather than absolute, standard of supply chain due diligence. The IFC stated that it intended to address supply chain performance assessment and verification in the upcoming Performance Standards review, demonstrating the CAO’s agenda-setting role for the Performance Standards RSS scheme. The 2012 Performance Standards reflect the CAO’s and IFC’s views on supply chain assessment, so CAO cases can influence periodic reviews of the Standards.

The previous wording in Performance Standard 1 above was replaced with:

In the event of risks and impacts in the project’s area of influence resulting from a third party’s actions, the client will address those risks and impacts in a manner commensurate with the client’s control and influence over the third parties, and with due regard to conflict of interest.

Where the client can reasonably exercise control, the risks and impacts identification process will also consider those risks and impacts associated with primary supply chains, as defined in Performance Standard 2 (paragraphs 27–29) and Performance Standard 6 (paragraph 30).

Interestingly, one of the recommendations by the EPFI Steering Committee was clarification on supply chains under Performance Standards 1, 2 and 6, and this was addressed in the amended language of Standard 1.

The CAO’s ongoing dialogue with the IFC regarding the Performance Standards promotes responsiveness to the interests of project-affected people. The CAO’s view of the IFC Performance Standards is informed by its consideration of complaints, making it better informed about the disregarded interests of project-affected people. In the Wilmar case, the CAO took a broader view of IFC-financed project impacts in light of arguments for those affected by oil palm plantations. The Dinant compliance audit provides a further opportunity for the CAO to interpret the Performance Standards and to comment on the Framework and Strategy. The audit concerns the 2006 Performance Standards, not the 2012 Standards or Framework and Strategy, which did not exist at the time of the events that gave rise to the complaint. However the CAO could decide to make guiding observations about both documents as it did in the Wilmar case regarding the scope of the RSPO Principles and Criteria and Performance Standards.

4. Importance of Participation

The palm oil case studies show that participation in the review process by project-affected people can overcome the problem of disregarded interests. Interactions between NGOs, CAO and IFC promoted responsiveness of the World Bank

196 Id.
197 Id.
199 IFC PS review team meeting with the EPFI Steering Committee — London, October 12: Summary of Discussion, supra note 84.
Group to the interests of palm oil project-affected people, prompting and informing the Framework and Strategy. These kinds of interactions are not possible with EPFIs due to the lack of transparency prior to Equator Principles III, and the lack of a review body. This part of the paper argues for the importance of responsiveness-promoting measures in the Equator Principles RSS scheme, the value of independence for review mechanisms in light of the RSPO, and the importance of promoting such measures for the IFC in its role as a promulgator of standards.

4.1. **Sustainability Standards Should Promote Responsiveness**

The improved transparency requirements of Equator Principles III will make it easier to monitor EPFIs, but a review mechanism is needed to enable the kind of participation by project-affected people currently possible in the Performance Standards RSS scheme as shown in the palm oil case studies. It is important that a review mechanism be as independent as possible from the subject(s) of review in order to be legitimate and effective, as illustrated by the difference between the CAO and RSPO review mechanisms.

EPFIs should follow GAL principles because the Equator Principles espouse standards aimed at the interests of project-affected people and therefore have a public quality, even though EPFIs are generally private institutions. The Equator Principles contain measures aimed at promoting the responsiveness of borrowers to project-affected people. The logical extension of the GAL principles underlying those measures is that the Equator Principles should also include measures to promote EPFI responsiveness. In addition, the Principles are based on the normative standards of the IFC Performance Standards that uphold the interests of project-affected people, so the governance measures should not allow EPFIs to disregard the interests of project-affected people, as is currently the case.

Furthermore, in order for the Equator Principles RSS scheme to claim to be based on the same standards as the IFC Performance Standards RSS scheme, there is an implicit requirement that EPFIs be subject to governance similar to the IFC. Part of the legitimacy of the IFC Performance Standards comes from the responsiveness-promoting measures to which the IFC is subject. The Equator Principles seek to gain legitimacy by incorporating the Performance Standards. However, without responsiveness-promoting measures, the Equator Principles RSS scheme is merely a cynical exercise that pays lip service to the Performance Standards without measures to promote EPFI responsiveness to project-affected people.

In addition, the RSPO review mechanism demonstrates the importance of independence for a review mechanism. The RSPO complaints process is ultimately subject to the politics of the Executive Board, whereas the CAO has the independence to make adverse findings and the power to rigorously monitor post-complaint compliance. A review mechanism risks giving rise to accusations of green washing without the independence to make formal adverse findings and rigorously monitor compliance.
4.2. **Sustainability Standard Promulgation Should Include GAL**

The IFC should promote GAL principles to protect its legitimacy as a promulgator of sustainability standards that aim to protect the interests of project-affected people.

The Equator Principles have been seen as an example of successful standard-setting for the financial sector by the IFC via promulgation of its Performance Standards through the Equator Principles.200 There has been much focus on the role of the IFC in setting sustainable development standards, however this discussion risks conflating the IFC’s standards-promulgation with its standards-setting. 201 The IFC promulgates its standards through outreach activities to encourage banks to adopt the Equator Principles. Prior to 2007, the IFC encouraged adoption through syndication activities in which it co-finances projects with commercial banks.202 Since 2007, the IFC has hosted an annual Community of Learning event attended by 80-100 banks.203 Furthermore, the IFC and EPFIs coordinate outreach activities in emerging markets,204 allowing the IFC to “extend its reach with commercial banks in those regions more easily.”205

The IFC’s role as standards-promuligator loses legitimacy without governance measures accompanying the normative sustainability standards to promote EPFI responsiveness. The IFC allows its standards to be used in the Equator Principles RSS scheme, which does not promote responsiveness because it has lacked adequate transparency standards and continues to lack a review mechanism. The IFC’s strategy to promote sustainability through promulgation of its Performance Standards provides only empty promises to project-affected people if there are no adequate responsiveness-promoting governance measures. The use of the IFC Performance Standards without responsiveness-promoting measures simply legitimizes the investments and profits of EPFIs while casting the IFC in a duplicitous light for its promulgation of standards.

NGOs and the CAO recognize the importance of GAL principles for EPFIs, and the CAO has recommended that the IFC advise EPFIs on improving accountability. NGOs, particularly BankTrack, have advocated for GAL principles such as transparency and review since the establishment of the Equator Principles.206 BankTrack, an international network of civil society organizations

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201 Wright, supra note 51, 62-67.
202 Wright, supra note 51, 62-67; Park, supra note 200, 551 (this mode of promulgating sustainability norms preceded the establishment of Equator Principles).
and individuals,\(^{207}\) has expressed frustration at the inadequate response of the Equator Principles regime.\(^{208}\) If EPFIs establish a grievance mechanism, NGOs will probably have more influence on EPFIs from the capacity to file complaints, as they do through the CAO mechanism. The CAO recently recommended that the IFC promote environment and social standards in the financial sector by advising “the EPFI network on issues such as [...] how to strengthen their transparency and accountability.”\(^{209}\) The IFC will improve its legitimacy as a standard-promulgator if it follows the CAO’s advice.

5. Conclusion

Differences between the membership of the IFC, Equator Principles and RSPO lead to noticeable differences between the RSS schemes. The IFC’s member states encourage its acceptance of GAL, whereas EPFIs as private financial institutions resist GAL asserting that the Equator Principles’ voluntary nature justifies non-application of GAL principles. The RSPO’s mixed membership gives rise to acceptance of GAL principles, but reluctance to relinquish control over potentially damaging outcomes for members.

This paper’s account of the IFC Performance Standards and Equator Principles RSS schemes is in many ways an account of NGOs influencing the IFC and private financial institutions to leverage the control of financiers over development projects to improve the sustainability of development. Both RSS schemes were established following NGO campaigns, and reforms to the schemes respond to further NGO campaigns.\(^{210}\) The operation of the IFC Performance Standards and Equator Principles RSS schemes relies on monitoring and enforcement by NGOs making claims to the CAO and running public campaigns, respectively. Interactions between institutions are also stimulated by NGOs. For example the CAO largely relies on complaints from NGOs to perform its review function, and the IFC relies on NGO campaigns to motivate EPFIs to engage with the IFC’s Performance Standards. On the other hand, NGOs rely on the CAO to legitimate their claims and interpretation of standards, and rely on the IFC to be a powerful sustainable development advocate with legitimacy in the private sector.

The roles and interactions of RSS scheme institutions and actors identified in this paper are likely to be observable elsewhere. For example, were EPFIs to establish a complaints mechanism, it would probably rely on NGOs’ monitoring...
activities and complaints to undertake its review function. Further, the IFC seems likely to continue its role as a setter and promulgator of standards, including through its engagement with the RSPO. The CAO appears set to continue to influence these other RSS schemes through its interactions with the IFC.

Governance measures reflecting GAL principles, such as transparency and review, facilitate the interactions and participation considered in this paper and thus promote the responsiveness of sustainable development RSS schemes to the interests of people affected by development projects. The palm oil industry continues to grow as the demand for food grows, and concerns about climate change will further stimulate this growth if biofuels are pursued more extensively as an alternative energy source. This growth threatens the interests of people living in areas with potential for oil palm plantation expansion. Accordingly, measures based on GAL principles that promote responsiveness to the interests of people who would be affected by such expansion are crucial to any RSS schemes that may apply to palm oil projects, including specific RSS schemes like the RSPO, and more general schemes such as the Equator Principles.

However, complaints mechanisms do not guarantee sustainable outcomes. The RSPO’s response to the Wilmar cases demonstrates the need for independence and strong monitoring powers. The Dinant case illustrates the risk that lessons will be learned and ignored by institutions.