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## Terms of Reference for Compliance Investigation of IFC’s Environmental and Social Performance in relation to its Investment in Wings Group’s PT SMU, Indonesia

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IFC Project #32208

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### About CAO and the Compliance Function

The Office of the Compliance Advisor Ombudsman (CAO) is an independent recourse and accountability mechanism for people and communities affected by projects financed by the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA). CAO works to address complaints fairly, objectively, and constructively while enhancing the social and environmental outcomes of IFC and MIGA projects and fostering public accountability and learning at these institutions.

CAO’s independence and impartiality are essential to fostering the trust and confidence of stakeholders involved in complaint processes. CAO is independent of IFC and MIGA management and reports directly to the IFC and MIGA Boards.

CAO carries out its work in accordance with the IFC/MIGA Independent Accountability Mechanism (CAO) Policy (“the CAO Policy”). Its three functions are shown below. For more information, visit: [www.cao-ombudsman.org](http://www.cao-ombudsman.org).

#### Dispute Resolution

CAO helps resolve issues raised about the environmental and/or social impacts of projects and/or sub-projects through a neutral, collaborative, problem-solving approach and contributes to improved outcomes on the ground.

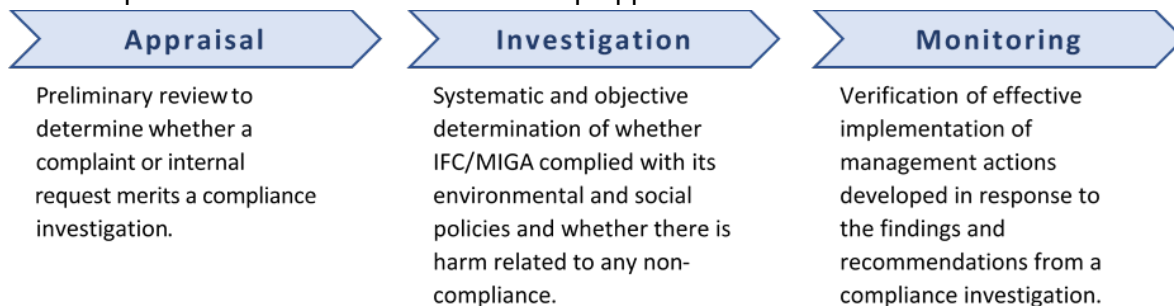
#### Compliance

CAO carries out reviews of IFC/MIGA compliance with the E&S policies, assesses related harm, and recommends remedial actions to address non-compliance and harm where appropriate.

#### Advisory

CAO provides advice to IFC/MIGA and the Boards with the purpose of improving IFC’s/MIGA’s systemic performance on environmental and social sustainability and reducing the risk of harm.

CAO’s compliance function follows a three-step approach:



## Context and Investment

Between 1997 and 2008, IFC financed 14 investments in the Wings Group,<sup>1</sup> a vertically integrated business group that manufactures and distributes consumer goods. The Group has its origins in the soap and detergent business, which relies on palm oil derivatives, and produces palm oil and other raw materials at its own plantations.<sup>2</sup> In 2011, Wings Group subsidiary PT SMU was one of the two “laundry giants” in Indonesia with over 40-percent market share.<sup>3</sup>

In 2012, the Wings Group launched a US\$176 million project to expand the products and capacity of four companies,<sup>4</sup> including PT SMU. In April 2013, IFC received Board approval for an A loan of US\$44 million and a syndicated B loan of US\$44 million to the four entities.<sup>5</sup> IFC’s rationale for the investment included supporting a longstanding client in reaching low-income consumers.

IFC’s financing for the detergent company PT SMU consisted of an A loan of US\$13.75 million and a B loan of US\$13.75 million. On December 16, 2019, PT SMU prepaid all outstanding IFC loan balances, ending IFC’s exposure to the subsidiary company.

Notably IFC’s investment in PT SMU was prepared shortly after the release of the 2011 World Bank Group (WBG) Framework and IFC Strategy for Engagement in the Palm Oil Sector (WBG Framework and IFC Strategy).<sup>6</sup> This in turn followed a CAO 2009 audit of a downstream IFC investments in a major palm oil company in Indonesia,<sup>7</sup> which resulted in an 18-month global moratorium on new WBG palm oil sector investments from September 2009. Informed by a global stakeholder consultation, the WBG Framework and IFC Strategy committed IFC to support sustainable palm oil production in its lending activities.<sup>8</sup>

## The Complaint

In November 2018, CAO received a complaint from the Indonesia NGO AMAN Kaltim.<sup>9</sup> Submitted on behalf of Indigenous community members in Long Beluah and Long Lian, North Kalimantan, the complaint cited environmental and social (E&S) impacts from oil palm plantations owned by PT Gawi Makmur Kalimantan (PT Gawi), a Wings Group subsidiary. Specific allegations included pollution of drinking water sources and associated health impacts, as well as the clearance of Indigenous Peoples’ forest and seizure of their land without consultation or compensation, failure to establish agreed smallholdings, and failure to provide agreed development benefit.

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<sup>1</sup> IFC Disclosure website: <https://disclosures.ifc.org/> Relevant IFC project numbers are: 7508, 8414, 10233, 11696, 23922, 24904, 25103, 25841, 26210, 27157, 17159, 27160, 27128, and 27129.

<sup>2</sup> Sayap Mas Utama PT in Home Care (Indonesia), May 15, 2015. Euromonitor Local Company Profiles, Euromonitor International. Also, Wings Group website: <https://wingscorp.com/>

<sup>3</sup> Laundry Care in Indonesia, September 17, 2012. Euromonitor Sector Capsules, Euromonitor International.

<sup>4</sup> Aside from PT SMU, IFC’s investment in the other three Wings subsidiaries were: PT Tirta Alam Segar and PT Murni Alam Segar to expand their beverage product lines, and PT Harum Alam Segar to commission a greenfield coffee mix production. IFC, Summary of Investment Information (SII) for IFC project no. 32208, 2012. Available at: <https://bit.ly/Wings01-SII>.

<sup>5</sup> IFC, SII, 2012.

<sup>6</sup> World Bank Group Framework and IFC Strategy for Engagement in the Palm Oil Sector, 2011. Available at: <https://bit.ly/WBG-IFCStrategyPalmOil>

<sup>7</sup> CAO Audit of IFC’s Investments in: Wilmar Trading (IFC No. 20348), Delta-Wilmar CIS (IFC No. 24644), Wilmar WCap (IFC No. 25532), and Delta-Wilmar CIS Expansion (IFC No. 26271), June 19, 2009. Available at: <https://officecao.org/Wilmar01Audit>

<sup>8</sup> WBG Framework and IFC Strategy, p. 31.

<sup>9</sup> See Annex 1 for a copy of the complaint.

PT Gawi received IFC financing in 2001–2007 but was not financed by IFC at the time CAO received the complaint. However, CAO accepted the complaint on the basis that IFC’s then client, PT SMU, sourced refined palm oil derivatives (oleochemicals) from refineries that in turn sourced some of their palm oil from PT Gawi mills and plantations.

## **Investigation Terms of Reference**

Where, as in the present case, the CAO appraisal process results in a decision to investigate, CAO’s appraisal report includes terms of reference for the compliance investigation, outlining:

- a. *The objectives and scope of the investigation;*
- b. *Any limitations on the scope of the investigation that may be appropriate, considering, among others, issues closed at the appraisal stage, the presence of concurrent judicial proceedings, or an IFC/MIGA Exit;*
- c. *The approach and method of investigation, and specific consultant qualifications; and*
- d. *A schedule for the investigation tasks, timeframe, and reporting requirements. This schedule will include deadlines for the submission of information by IFC/MIGA to inform the compliance investigation process.*<sup>10</sup>

## **Objective and Scope of the Compliance Investigation**

As established in CAO’s Appraisal Report, CAO will conduct a compliance investigation of IFC’s investment in PT SMU of the Wings Group as it relates to the complaint. The investigation will determine whether IFC complied with its E&S Policies relevant to the investment and whether there is harm related to any IFC non-compliance. In determining whether IFC has complied with its E&S Policies, CAO will include, where appropriate, an assessment of whether IFC deviated in a material way from relevant directives and procedures.

Relevant to the issues raised in the complaint, the objective of the investigation is to determine:

1. Whether IFC has complied with its E&S Policies, including:
  - a. Whether IFC conducted pre-investment E&S due diligence and supervision of its investment in PT SMU as required by the Sustainability Policy, and the adequacy of such due diligence and supervision;
  - b. Adequacy of IFC’s review and supervision of PT SMU’s compliance with IFC’s Performance Standards; and
2. Whether there is harm or potential harm related to any IFC non-compliance.<sup>11</sup>

The investigation will consider whether IFC properly applied the following Sustainability Framework requirements to the project:

- Whether IFC properly applied its Sustainability Policy requirement for pre-investment E&S due diligence, including a review of reputational and third-party risks, a supply chain assessment, and assessment of the client’s control and leverage over its supply chain (Sustainability Policy, paras. 21 and 23; also ESRP 2009, para. 2.2.4).

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<sup>10</sup> CAO Policy, para. 118.

<sup>11</sup> Ibid., paras. 112–114.

- Whether IFC assured that Board approval of the project was informed by an assessment of E&S risks and impacts in PT SMU's supply chain, including relevant ESAP items or E&S conditions of disbursement in accordance with para. 21 of the Sustainability Policy.
- Whether IFC verified the client's review of third-party risks with a view to creating outcomes consistent with Performance Standards PS3, PS4, PS5, PS6, and PS7 in accordance with para. 23 of the Sustainability Policy.
- Whether IFC verified the proper application of PS1, para. 10, to the project in relation to E&S risks and impacts from primary supply chains, including requiring the client to conduct supply chain mapping and risk assessment.
- Whether IFC properly applied Sustainability Policy requirements to the project during supervision in terms of reviewing project-related information that became known and, on the basis of that information, provide advice to the client on managing the E&S issues, per IFC ESRP (2013) 6.2.1.
- Whether IFC properly applied Policy requirements for project supervision during the life of the PT SMU investment, including prior to prepayment by its client, to ensure that its investment is implemented in accordance with the Performance Standards requirements. The Performance Standards require application of a mitigation hierarchy, requiring its client to assess and mitigate/compensate for any residual impacts, per Sustainability Policy, paras. 6–7.

In relation to any IFC non-compliance with these E&S requirements, the investigation will consider whether there is related harm or potential harm to the complainants.

### **Methodological Approach**

CAO will base the compliance investigation on information available to CAO from interviews, statements, reports, correspondence, CAO observations of activities and conditions, and other sources that CAO deems relevant.<sup>12</sup>

The compliance investigation process and compliance investigation report will include:

- a. The investigation findings with respect to compliance, non-compliance, and any related harm.*
- b. Context, evidence, and reasoning to support CAO's findings and conclusions regarding the underlying causes of any non-compliance identified.*
- c. Recommendations for IFC/MIGA to consider in the development of a Management Action Plan (MAP) relating to the remediation of Project- or Sub-Project-level non-compliance and related harm, and/or steps needed to prevent future non-compliance, as relevant in the circumstances. In case of a project where the IFC/MIGA Exit has occurred, recommendations will take into account the implications of such an IFC/MIGA exit.<sup>13</sup>*

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<sup>12</sup> Ibid., paras. 115 and 117.

<sup>13</sup> Ibid., para. 120.

Sufficient, relevant evidence is required to afford a reasonable basis for CAO's compliance findings and conclusions. CAO will assess whether there is evidence that IFC/MIGA applied relevant E&S requirements considering the sources of information available at the time the decisions were made, and will not make findings and conclusions with the benefit of hindsight.<sup>14</sup>

### **External Expert(s)**

As per its established practice, CAO will engage one or more external experts for this investigation. For this compliance investigation, CAO considers the following qualifications as necessary:

- Significant expertise in agricultural supply chain issues, preferably with familiarity with the soap/detergent or similar industry;
- Significant expertise in conducting supply chain assessments in relation to E&S issues;
- Significant experience in and knowledge of the palm oil sector, preferably in Indonesia;
- Knowledge of IFC's E&S policies, standards, and procedures, particularly the 2012 Sustainability Policy and the 2012 Performance Standards;
- Experience and knowledge relevant to conducting compliance investigations;
- Demonstrated ability to analyze policies and practices and develop proposals for reform in complex institutional contexts; and
- Fluency in English, familiarity with Bahasa desirable.

### **Field Visit and Potential Limitations of the Investigation**

A field visit to the complainants' communities and relevant Wings Group facilities is anticipated during the compliance investigation, including Wings Group plantations if possible. Given that IFC no longer has an ongoing financial relationship with the Wings Group, access to relevant facilities may be limited. For such a visit, the CAO case team, external experts, and an interpreter/translator would be expected to participate.

### **Compliance Investigation Schedule, Timeframe, and Reporting Requirements**

According to the CAO Policy,<sup>15</sup> a draft compliance investigation report must be circulated within one year of the disclosure of an appraisal report. By April 2024, a draft compliance investigation report for this case will be circulated to IFC management and all relevant departments for factual review and comment. Management may share the draft report with the client on the condition that appropriate measures are in place to safeguard the confidentiality of the draft report prior to public disclosure.<sup>16</sup> IFC will have 20 business days to provide written comments.

At the same time, the draft investigation report will be circulated to the complainants for their factual review and comment, provided that appropriate measures are in place to safeguard the confidentiality of the draft report prior to public disclosure. If such confidentiality measures are not in place, complainants will, at a minimum, receive a draft table of the investigation's findings for

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<sup>14</sup> Ibid., paras. 116–117.

<sup>15</sup> Ibid., para. 121.

<sup>16</sup> Ibid., para. 122.

factual review and comment and as a source of information to inform future consultations on any IFC Management Action Plan (MAP).<sup>17</sup>

Upon receiving comments on the consultation draft from IFC and the complainants, CAO will finalize the investigation report. The final report will be submitted to IFC senior management and circulated to the Board for information. The Board has no editorial input on the content of a CAO compliance investigation report. Once the investigation report is officially submitted to IFC management and circulated to the Board, CAO will notify the public on its website of the investigation's completion.<sup>18</sup>

Upon CAO's final submission of the compliance investigation report to IFC, IFC management has 50 business days to submit a management report to the Board for consideration. The management report must include a MAP for Board approval. A MAP contains time-bound remedial actions that IFC proposes for the purpose of addressing CAO findings of non-compliance and related harm. IFC must consult with complainants and the client during its MAP preparation process, and its management report must also include a reasoned response to CAO's finding or recommendations regarding non-compliance or related harm that IFC is unable to address in the MAP.<sup>19</sup>

CAO will submit comments on the proposed MAP to the Board, and the complainants may submit a statement to CAO on the proposed MAP and the adequacy of consultations for circulation to the Board.<sup>20</sup> Upon the Board's approval of the MAP, the compliance investigation report, management report, and MAP will be published on CAO's website.<sup>21</sup>

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<sup>17</sup> Ibid., para. 124–125.

<sup>18</sup> Ibid., paras. 123, 127–129.

<sup>19</sup> Ibid., paras. 130–132, 134.

<sup>20</sup> Ibid., para. 135.

<sup>21</sup> Ibid., para. 138.