

To the Ministry of Finance

19 May 2014

UNOFICIAL ENGLISH TRANSLATION

Recommendation to exclude IJM Corporation Berhad from the investment universe of the Government Pension Fund Global

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1 Summary

The Council on Ethics for the Government Pension Fund Global (GPF) recommends the exclusion of IJM Corporation Berhad (IJM) and its subsidiary IJM Plantations Berhad (IJM Plantations) from the investment universe of the GPF. At the end of 2013, the GPF owned shares in IJM valued at USD 12 million, equivalent to an ownership interest of 0.49%. The GPF currently holds no shares in IJM Plantations.

The Council on Ethics has assessed whether there is an unacceptable risk of IJM being responsible for severe environmental damage in connection with its subsidiary IJM Plantations' development of oil palm plantations in Indonesia.

The Council has examined four concession areas currently being established by IJM Plantations in East Kalimantan. These concession areas cover approximately 35,000 ha in total, and lie in an ecoregion known for its rich biodiversity and large number of endemic and endangered species. The Council's investigations indicate that the company converted around 10,000 ha of lowland rainforest into palm oil plantations in the period 2008–2012. Conversion appears to be ongoing. It also appears that the company has cleared forest in buffer zones outside the concession boundaries in one of the investigated areas.

IJM has not provided any information on the locations of its concessions, or on forest condition and biodiversity. Accordingly, no concrete information is available on the biodiversity that will be lost through conversion. The Council on Ethics has emphasised that the company appears to be taking no steps to reduce the loss of biodiversity, and the fact that IJM Plantations does not appear to be conducting High Conservation Value assessments in the concessions – a potentially important means of reducing biodiversity loss in connection with forest conversion. The company has stated that it plans to begin working towards RSPO (Roundtable for Sustainable Palm Oil) certification in 2018. In the Council's view, this is an unusually long timescale for building a more sustainable operation. The company's continuing conversion without implementing measures to ensure the conservation of important ecological values in the concessions increases the risk of severe environmental damage.

The Council has contacted the company several times with questions about its operations, including what steps the company is taking to mitigate the environmental damage associated with the conversion of forest into plantations, but has received no answers to these. The Council is of the opinion that the company's unwillingness to provide information reinforces the basis for the recommendation to exclude the company.

The conversion of natural forest and habitats into oil palm plantations entails irreversible alteration of ecosystems and vegetation, with major consequences for biodiversity. This is occurring in a threatened ecoregion known for its rich biodiversity. The company does not seem to be implementing measures to prevent the loss of important conservation values, and does not wish to provide information on its efforts to mitigate impacts in future. Following an overall assessment, the Council on Ethics has concluded that there is an unacceptable risk of severe environmental damage resulting from IJM's plantation operation.

2 Introduction

The Council on Ethics has assessed the GPF's investments in the company IJM Corporation Berhad (IJM) against the Guidelines for Observation and Exclusion of companies from the investment universe of the Government Pension Fund Global (the ethical guidelines).

At the end of 2013, the GPFG owned shares valued at USD 12 million in IJM, corresponding to an ownership interest of 0.49%. The GPFG currently holds no shares in IJM Plantations.

2.1 What the Council has assessed

The Council's assessment concerns IJM's subsidiary, IJM Plantations, which is developing oil palm plantations in Indonesia. The Council has assessed whether there is an unacceptable risk that IJM contributes to or is itself responsible for severe environmental damage as per paragraph 2, section three of the Ethical Guidelines.

In previous recommendations regarding severe environmental damage, the Council has put particular emphasis on whether:¹

- the damage is significant;
- the damage causes irreversible or long-term effects;
- the damage has considerable negative impact on human life and health;
- the damage is a result of violations of national laws or international norms;
- the company has neglected to act in order to prevent the damage;
- the company has not implemented adequate measures to rectify the damage;

Environmental impacts associated with the clearing of tropical forests

Commercial logging and the conversion of tropical forest into plantations are considered to be some of the most important threats to the preservation of ecosystems and biological diversity; they also contribute significantly to greenhouse gas emissions. Deforestation and forest degradation accounted for about 10 per cent of global greenhouse gas emissions in the period 2000 and 2009.²

Conversion involves the felling of trees and the removal of other vegetation before an area is used to set up plantations for the production of palm oil, lumber or other monocultures. Such mono-cultures are of limited ecological value compared to natural forests.

Both the UN, the World Bank and national governments have recognized the need to reduce deforestation and forest degradation, through *inter alia*, the establishment of the United Nations Collaborative Initiative on Reducing Emissions from Deforestation and Forest Degradation (REDD and REDD+) supported by the World Bank and others. The Norwegian Government has also supported these initiatives by allocating up to three billion NOK a year to efforts to reduce deforestation in developing countries. These schemes are also considered to benefit biodiversity and sustainable development.

Indonesia is one of the countries that Norway is collaborating with under the REDD+ Scheme. Indonesia is home to the world's third-largest tropical forest and has some of the highest deforestation rates in the world. Between 1990 and 2010, Indonesia lost 20 per cent of its forest cover, or more than 24 million ha.³ In Kalimantan, where IJM's license areas are located, the conversion of forests to oil palm plantations has been a leading driver of deforestation. The development of plantations is also a future threat to important ecological areas and biodiversity in the region. Based on present allocated leases by the government, full development would

¹ See e.g. the Council's recommendations regarding Ta Ann Berhad, Samling Global og WTK Berhad, available at www.etikkradet.no.

² IPCC (2013): Climate Change 2013. *The Physical Science Basis. Working Group I contribution to the IPCC 5th Assessment Report* <http://www.ipcc.ch/report/ar5/wg1/#.Um6XYDhFD5o>

³ <http://rainforests.mongabay.com/deforestation/2000/Indonesia.htm>. Data based on UN FAO State of the World's Forest.

convert up to 9.4 million ha of land by 2020, of which 90 per cent is forested land, including 41 per cent intact forest.⁴

The conversion of peatlands is an Indonesia-specific challenge, as Indonesia accounts for almost 60 per cent of global greenhouse gas emissions from peat decomposition.⁵ In addition to being important carbon sinks, peatlands also represent unique ecosystems with regard to biodiversity. In 2010, Norway entered into a partnership with Indonesia to support the country's efforts to reduce deforestation, forest degradation and destruction of peatlands. Under this agreement, Indonesia implemented a nationwide moratorium on new forestry and plantation concession, which aims to reduce new clearing of primary forests and peat lands. The moratorium was set to expire in May 2013, and has been extended for two more years. The moratorium is part of Indonesia's efforts to reduce its carbon emissions by 26 per cent by 2020.

The Council's point of departure is that tropical forests of Indonesia are among the most biodiverse ecosystems on earth. In addition to supporting this biodiversity and providing habitats for many endangered species, the tropical forest also plays an important role in providing fundamental eco-system services, such as carbon storage, water management and protection against erosion. Tropical forests are important for the state of the environment globally, and deforestation and forest conversion are major threats to the future existence of these ecosystems. Accordingly, and taking into account the many international and national initiatives taken to reduce deforestation and the degradation of tropical forest, the Council has assessed the risk of environmental damage associated with the clearing of tropical forests. In its assessment, the Council emphasises the scale of the clearing, to what extent the company's licence area overlaps with areas of important ecological values, and which consequences the conversion of forest will entail for endangered species and their habitats.

2.2 Sources

Little public information is available on IJM's plantation operations or the environmental impact of the company's conversion of tropical forest. The Council on Ethics has requested information from the company, including the locations of the concessions, the state of the forest in the concessions, environmental impact assessments and surveys of conservation values in the concessions (High Conservation Value (HCV) area assessments). IJM has not responded to the Council's enquiry.

The Council has therefore conducted its own investigations to locate the company's concessions. The Council has also attempted to clarify whether IJM Plantations' concessions lie in ecologically important areas, whether forest will be converted and whether such conversion may entail the loss of endangered species and their habitats. The data and sources used include information from the company's website, satellite imagery, various types of maps (vegetation maps showing forest types and peatlands, and maps showing areas included in the Norway-Indonesia moratorium), public information from national and local authorities in Indonesia, and academic literature. However, these have not provided details of the state of the forest or biodiversity in the individual concessions.

⁴ Kimberly M. Carlson, Lisa M. Curran, Gregory P. Asner, Alice McDonald Pittman, Simon N. Trigg and J. Marion Adeney 2012. Carbon emissions from forest conversion by Kalimantan oil palm plantations. *Nature Climate Change*. 2012

⁵ Fact Sheet Norway-Indonesia Partnership REDD+, <http://www.norway.or.id/PageFiles/404362/FactSheetIndonesiaPeatMay252010.pdf>.

3 About IJM Corporation Berhad and IJM Plantations Berhad

IJM’s main operations include construction and engineering, infrastructure, property development, stone quarrying and cement production, and plantations.⁶ The company is listed on Bursa Malaysia in Kuala Lumpur.

The group began developing oil palm plantations in 1985. The plantation business is owned and operated by the subsidiary IJM Plantations, in which IJM has a 55.11 per cent stake. IJM Plantations is also stock-exchange listed in Kuala Lumpur. The GPFG currently holds no shares in this company.

IJM’s plantation operation was originally based in Sabah, Malaysia, where the company has 11 plantations totalling 30,000 ha.⁷ These appear to be fully developed. Due to a lack of new land, IJM Plantations expanded its operation to Indonesia.⁸ The company holds majority stakes in five plantations in Indonesia, the most recent of which was bought in 2012. One plantation has been fully developed, while the four others are currently under development. All of these lie in the province of East Kalimantan. IJM Plantations’ plantations in Indonesia total 54,000–72,000 ha.⁹

4 The Council on Ethics’ investigations

The Council on Ethics has focused on newly established plantations where forests and peatlands are being, or have recently been, converted. The investigations cover the period 2008–2012 (or up to the present day where data are available). Table 1 provides an overview of the four concessions in Indonesia where the company is currently establishing new plantations, while Figure 1 shows their locations in East Kalimantan.

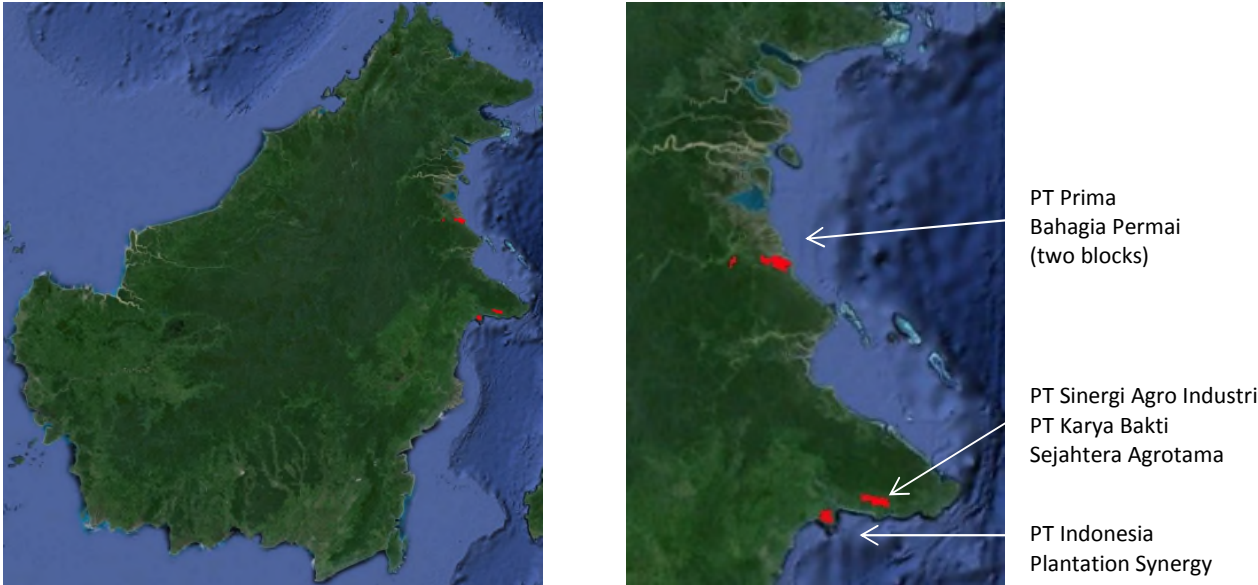


Figure 1: Locations of four IJM Plantations concessions in East Kalimantan, Indonesia, investigated by the Council on Ethics

⁶ IJM Corporation website <http://www.ijm.com/web/aboutUs/corpProfile.html>.
⁷ IJM Plantations Annual Report 2012 and Annual Report 2013.
⁸ IJM Plantations Annual Report 2007.
⁹ The lower estimate is taken from Malaysia Corporate Digest, 26 September 2012: IJM Plantations Yields Set To Stabilise With 95% Acquisition Of KBSA” (land bank in Sabah subtracted from reported total land bank (82,763 hectares). According to an AmResearch company report on IJM Plantations (17 April 2013), “the size of IJMP’s landbank in Indonesia is estimated at 71,660 ha”, <http://cdn1.i3investor.com/my/files/dfgs88n/2013/04/17/1478340610-1344853001.pdf>.

IJM Plantations' concession areas in Indonesia appear to lie in the Bornean Lowland Rainforest Ecoregion, which is included in the WWF's Global 200 Priority Eco-regions¹⁰ list due to its usually rich biodiversity and because it is regarded as threatened, not least by the conversion of forest into plantations.¹¹ In its natural state, the Bornean lowland rainforest is considered particularly species-rich, being home to numerous bird and plant species (380 and 10,000 species, respectively), and a high proportion of endemic and endangered species such as the Bornean orangutan (*Pongo pygmaeus*).

All four concession areas lie in areas previously covered by lowland forest. In total, it appears that approximately 10,000 ha of lowland forest have been converted in the concession areas in the period 2008–2012 (see Table 1). Since IJM has not provided any information, the Council has no concrete data on the state of the forest in the concession areas, or whether the concessions do in fact contain important conservation values or are habitats for endangered species, or on the importance of the remaining forest areas in the landscape.

Table 1: IJM Plantations concessions in Indonesia assessed by the Council on Ethics

Subsidiary/location	Concession area in hectares		Cleared areas in the concession, 2008–2012, hectares	Concession area status in 2012
	As per maps ¹²	Annual report ¹³		
PT Indonesia Plantations Synergy	5,900	20500	0	In 2010, the concession area appeared to comprise agricultural areas used by local communities, with no residual forest. Conversion of the area has started.
PT Karya Bakti Sejahtera Agrotama	1,300		7,100	The concession lies directly south of PT Sinergi Agro Industri (see below). The entire area was covered by lowland forest, and was fully cleared between 2008 and 2012. ¹⁴
PT Sinergi Agro Industri	10,100			Until recently, the concession area was covered by forest. Dense-canopy lowland forest was being cleared in 2012.
PT Prima Bahagia Permai	15,900	17,000	3,300	Almost 3,300 ha of lowland forest were converted in the period 2008–2012. The remaining forest in the concession areas is likely to be cleared.

In Kalimantan, much of the landscape and habitats have suffered many years of degradation, and the forest has been fragmented in the areas in which IJM's concessions are located. As a consequence, the species diversity and ecosystems that were once found in the area have been impacted for several years, and important values may already have been lost. On the other hand, this may also mean that precisely the forest areas that remain in the concessions have important ecological functions. Based on the locations of the concessions and other available information,

¹⁰ The Global 200 is a list of ecoregions identified by the World Wildlife Fund (WWF) as priority areas for conservation. An ecoregion is defined as "a large unit of land or water containing a geographically distinct assemblage of species, natural communities, and environmental conditions". http://wwf.panda.org/about_our_earth/ecoregions/about/.

¹¹ Wikramanayake et al. (2002): *Terrestrial Ecoregions of the Indo-Pacific. A Conservation Assessment*. USA: Island Press. According to WWF, the Global Ecoregions is a science-based global ranking of the Earth's most biologically outstanding terrestrial, freshwater and marine habitats.

¹² Areas have been calculated using Google Earth Pro, based on maps of the concessions from the National Land Agency (BPN).

¹³ IJM Plantations *Annual Report 2013*.

¹⁴ According to IJM's website, PT KBS was incorporated as a 95% subsidiary on 25 January 2010, and fully acquired on 8 July 2013, www.ijm.com/web/aboutUs/ir_structure_karya.htm.

the Council has concluded that the concession areas are highly likely to contain important ecological values.

The PT Sinergi Agro Industri concession area was covered by dense forest until recently. The company is currently clearing the forest, and satellite images show that, with few exceptions, all vegetation along waterways and wetlands is being removed (see Figure 2).¹⁵ It is unclear to the Council whether this is illegal. However, maps from the National Land Agency¹⁶ show that border zones along waterways in the western half of the concession and buffer zones along roads (approximately 200m wide) are not included in the concession, indicating that the removal of forest in these areas is illegal (see Figure 2).

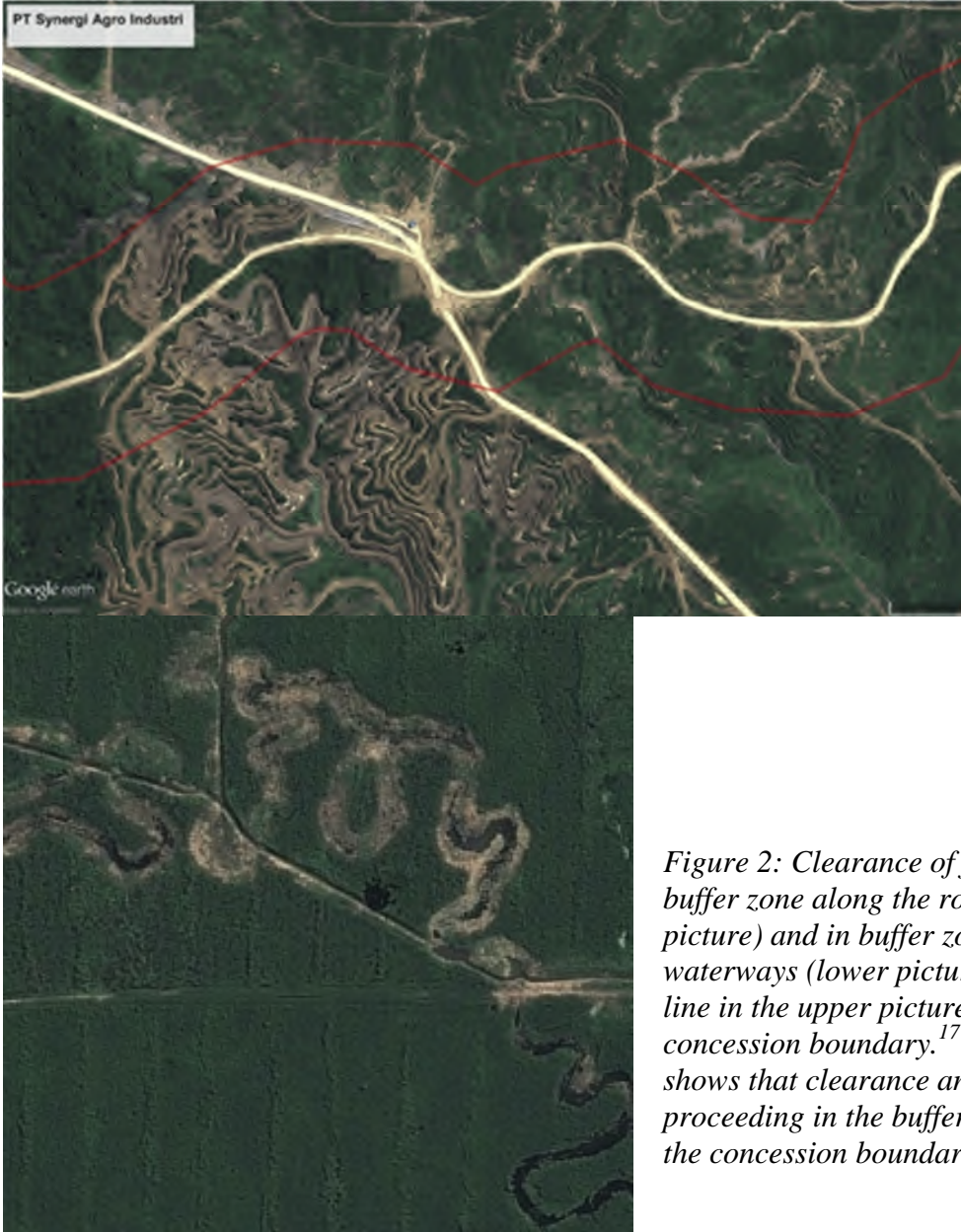


Figure 2: Clearance of forest in the buffer zone along the road (upper picture) and in buffer zones along waterways (lower picture). The red line in the upper picture shows the concession boundary.¹⁷ The picture shows that clearance and planting are proceeding in the buffer zone outside the concession boundary.

¹⁵ Google Earth, May 2010.
¹⁶ BPN cadastral map of the concessions.
¹⁷ Google Earth, May 2010.

5 Information from the company

5.1 The Council on Ethics' contact with IJM

The Council on Ethics contacted IJM in May and September 2012, requesting information about the environmental and social impacts of the company's plantation operations, including how the development of new plantations affects forests, ecosystems and biodiversity, and how forest in the concessions containing special conservation values has been identified and protected. The company did not reply to the Council.

In December 2013, IJM received a draft recommendation for comment. The company replied that it did not wish to comment on the recommendation.

5.2 IJM's position

In its Annual Report 2013, IJM Plantations wrote:

“Environmental stewardship has been embedded into our business model to ensure the long-term economic and environmental viability of our agricultural activities. The Group is committed to minimise the impact of its agricultural activities to the environment by pursuing green initiatives such as biodiversity conservation, enhancement and protection, responsible resource management and implementation of effective pollution prevention measures.”¹⁸

As regards conservation areas, the company has stated that it has “set-aside more than 8% or equivalent to 5,620 acres [2,327 ha] of its land bank in Sabah for the purpose of conservation, research and education. These conservation areas comprise of natural landscapes that includes wetlands, water bodies, hilly terrains, and secondary forest with high conservation values.”¹⁹

IJM Plantations has been a member of the Roundtable for Sustainable Palm Oil (RSPO) since September 2004. Thus far, none of the company's concessions has been certified. The company aims to achieve RSPO certification for the concessions by 2018.²⁰

6 The Council on Ethics' assessment

Based on the available information, the Council on Ethics has assessed whether there is an unacceptable risk of IJM being responsible for severe environmental damage through its subsidiary IJM Plantations' development of oil palm plantations in Indonesia. The Council has concentrated its assessment on four concessions in which forest and peatlands are currently being, or have recently been, converted into plantations.

Since IJM has not provided any information on the matter, the Council on Ethics has based its assessment on satellite imagery, various types of maps, other public information and academic literature. This information gives an indication of forest types and forest cover, but is not detailed enough to establish with certainty what ecosystems are in fact present in the concessions and their status, or what biodiversity will be lost as a result of conversion.

The four concessions investigated by the Council all lie in East Kalimantan. The Council's investigations indicate that the company converted around 10,000 ha of lowland forest into

¹⁸ IJM Plantations *Annual Report 2013*.

¹⁹ See footnote 18.

²⁰ RSPO website, www.rspo.org/sites/default/files/ACOP2012_GRW_1-0007-04-000-00-91.pdf

plantations in 2008–2012; most likely lowland rainforest in good condition. It also appears that the company is clearing forest in buffer zones outside the concession boundary in one of the investigated areas, an activity that is normally illegal. The scale of conversion thus far is not especially large, but conversion is ongoing and will continue. The Council has emphasised that the company's concessions lie in the Bornean Lowland Rainforest Ecoregion, which is known for its rich biodiversity and is particularly threatened by the establishment of new oil palm plantations. The Council also finds that the company's activities in this area appear to be inconsistent with national and international anti-deforestation initiatives.

IJM has provided little information on the steps it is taking to reduce the loss of biodiversity in connection with the development of plantations. The company does not appear to be conducting High Conservation Value assessments in its concession areas. Such assessments can be an important instrument for reducing biodiversity loss in connection with the conversion of forest. The company has stated that it intends to begin working towards RSPO certification in 2018. In the Council's view, this is an unusually long timescale for building a more sustainable operation. The company's continuing conversion without implementing measures to ensure the preservation and management of important ecological values in the concessions increases the risk of severe environmental damage.

The Council has contacted the company several times with questions about its operations, including what steps the company is taking to reduce the environmental damage associated with the conversion of forest into plantations, but has received no answers to these. The Council is of the opinion that the company's unwillingness to provide information reinforces the basis for the recommendation to exclude the company. In this regard, the Council refers to the white paper on the management of the government pension fund in 2008,²¹ in which the Ministry of Finance wrote the following, among other things:

“The Ministry finds that a lack of information about a company's behaviour, and not least the willingness of the company to contribute information by itself, can lead to the risk of contribution to unethical conduct being regarded as unacceptably high. In practice this could mean that the same documentary requirements for justifying an exclusion cannot be made in less transparent markets, where facts can be more difficult to prove.”

The company's conversion of natural forest and habitats into oil palm plantations entails irreversible alteration of ecosystems and vegetation, with potentially major impacts on biodiversity. This is occurring in a threatened ecoregion known for its unusually rich biodiversity. The company does not seem to be implementing measures to prevent the loss of important conservation values, and does not wish to provide information on its efforts to reduce harmful effects in future. Following an overall assessment, the Council on Ethics has concluded that there is an unacceptable risk of severe environmental damage resulting from IJM's plantation operation.

²¹ Report No. 20 to the Storting (2008-2009) – *On the Management of the Government Pension Fund in 2008*, textbox 4.6, <https://www.regjeringen.no/en/dokumenter/report-no.-20-to-the-storting-2008-2009/id553201/?ch=1>.

7 Recommendation

The Council on Ethics recommends the exclusion of the company IJM Corporation Berhad and its subsidiary IJM Plantations Berhad from the investment universe of the Government Pension Fund Global due to an unacceptable risk of the companies being responsible for severe environmental damage.

Ola Mestad
Chair

(Signature)

Dag Olav Hessen

(Signature)

Ylva Lindberg

(Signature)

Marianne Olsson

(Signature)

Bente Rathe

(Signature)