

Request for Inspection
of
Rondônia Natural Resources Management Project
(Loan No. 3444-BR)

Additional Review

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Introduction

1. The World Bank (“Bank”) approved the Loan to support the Rondônia Natural Resources Management Project—known as PLANAFLORO—in March 1992. Implementation of the social and environmental components of a series of Bank-financed projects of the 1980s—known as POLONOROESTE—had been neither adequate nor implemented. PLANAFLORO, intended to redress this failure, was designed in accordance with Bank strengthened environmental and social policies and procedures introduced in the late 1980s/early 1990s. The Staff Appraisal Report (“SAR”) and President’s Memorandum for PLANAFLORO convey Management’s belief that investments in the environment could pay off in economic terms. This was meant to be a showcase project for a new era in Bank lending for sustainable development.

The Request

2. The Executive Directors by creating the Inspection Panel (“Panel”) acknowledged the need for an independent mechanism to receive complaints from groups who believe they have been or will be directly and adversely affected by a Bank-financed project. In the case of this Request, communities previously adversely affected in Rondonia by the POLONOROESTE program expected beneficial effects from the implementation of PLANAFLORO according to the standards and timetable promised by the Bank, but expectations were not met. Therefore, on June 14, 1995, the intended beneficiaries represented by local non governmental organizations (“NGOs”) requested the Panel to investigate (“Request for Inspection”) the reasons for the Bank’s failure to carry out its commitment to prevent further damage to their land. The Requesters’ fundamental complaint is that the Project—intended to be beneficial to fragile communities and the natural environments they depend on for their livelihood—has not been adequately implemented since Board approval 3 1/2 years ago. Since the Closing Date of the Loan is December 31, 1996, it appears that just one year remains for such objectives to be achieved. Nevertheless, the Requesters fully supported such project objectives.

Management Response

3. The Management Response (“Response”) to the Request for Inspection (“Request”), submitted to the Panel on July 19, 1995, acknowledged a number of instances of lack of compliance with policies.

Panel Recommendation and Executive Directors’ Decision

4. On September 12, 1995 the Executive Directors considered the Panel’s recommendation (“Recommendation”) relating to the Request. The Panel recommended that: “the Executive Directors authorize an investigation into the violations of Bank policies and procedures alleged in the Request”

5. The Executive Directors “agreed that before a decision could be made by the Board on the Panel’s recommendation..., the Panel should conduct an additional review to further substantiate the materiality of the damages and to establish whether such damages were caused by a deviation from Bank policies and procedures.”

6. At the same time the Executive Directors “welcomed the project implementation and supervision mission planned to take place shortly, as well as Management’s commitment to provide periodic progress reports on the project.”

7. Management has provided the Panel with a draft Report by Regional Management entitled, “Brazil: Rondonia Natural Resources Management Project (Loan 3444-BR) -- Report on the Status of Implementation”, dated November 29, 1995 (“Draft Report”). The Draft Report was discussed in a meeting with Management on December 4, 1995.

Additional Review

8. This additional review responds to the Executive Directors’ request and takes into account subsequent information obtained by the Panel, including several Aide-Mémoire and Back-to-Office Reports (“BTO”) and the Draft Report. In this case the Panel has been asked to further review the past, meaning the period from inception of the project until the filing of the Request.

9. The Panel is presenting this additional review based on available data at this time because:

- Sufficient information is available to illustrate how the rights and interests of groups have been adversely affected and that they have suffered substantial, possibly irreversible, material damage.

- Damage continues and in some areas is worsening, but it could be mitigated in the future if Management takes steps to remedy the situation in high priority vulnerable areas--quickly.
- If authorized, an investigation to obtain specific data indicating and evidence quantifying monetary and other damage that occurred between 1992 and 1995 in all other relevant areas of the State of Rondonia, would take about six months. A “Work Plan” is attached as **ANNEX A**.
- It is imperative to set project priorities now to accelerate implementation of feasible remedial measures for this beneficial ongoing project. This may involve reorientation of goals and a revision of specific targets.

Materiality of Damages

Current Situation in Rondonia

10. The Requesters base their Request on perceived continuing damage to their livelihood, environment and cultural heritage. This Panel has confirmed this through local sources including intended project beneficiaries, news reports, satellite imagery, and other sources of information. However, information on the material impact of, for example, selective illegal logging of valuable trees, seasonal incursions, and physical intimidation can only be provided by court, police and other records, and first hand accounts through conduct of an investigation.

11. Local sources confirm damage claimed by the Requesters, and this includes information from interviews conducted by the Inspector who visited the Project area in August 1995. Photographs of damage in the reserves taken by the Inspector and others are available to the Executive Directors upon request. Furthermore, **ANNEX B** contains copies of records of illegal deforestation and seizure of stolen timber, notices, and citations issued by IBAMA, and letters sent to state and local authorities by rubber tapper organizations, regarding recent deforestation and invasions in the Extractive Reserve of Rio Cautario Area. The letters describe several incidents of violence against the families living in the Reserve Area.

12. Widespread public awareness of the situation in the Amazon—and in particular, Rondonia—has been the result of the many reports at the local, national and international level from 1993 onwards. Repeated claims of increasing damage and a worsening situation in the areas that are supposed to be properly established, demarcated and protected under PLANAFLORO have appeared in a number of publications. **ANNEX C** contains a sample of such local and national and international reports.

13. Material harm to affected parties in Rondonia is basically caused by four different activities:

- Illegal logging
- Illegal settlements accepted and promoted by INCRA
- Invasions of protected areas
- Burning

Illegal logging

14. By definition there is no authoritative data available at this stage but there is abundant evidence of illegal logging activities contained in many news items, and in

NGO reports. The Management Response to the Request and its current Draft Report recognize its widespread existence (see, for example, Draft Report, Annex A, paras. 14 & 29).

Illegal settlements accepted and promoted by INCRA

15. Illegal settlements have been widely reported by NGOs and inhabitants in Rondonia. Management also acknowledges that INCRA has allowed illegal settlement in areas that were supposed to be protected by the Project. For example the Report states:

“In spite of the Agreement signed between Rondonia and INCRA in November 1992¹ (condition of effectiveness), during the first two years of project implementation INCRA tended to pursue an independent path, often in contradiction to the requirements of Zoning. The State, for political reasons, was not able to obtain INCRA’s compliance with project objectives nor was it able to define the rules for joint State-INCRA action to ensure full compliance with Zoning in the implementation of the State’s land tenure policy. The result was that from 1992 to April 1995, INCRA attempted to establish seven land settlement in Zones 3, 4, and 5, and about 5% of land titles issued during that period were for land holdings in those Zones in direct conflict with provisions of the Zoning Law.” (Draft Report, Annex A, para. 4).

However, interview sources suggest that the figure of 5% appears conservative and does not either indicate how many titles were issued and the total size of the area illegally settled.

Invasions of protected areas

16. The Request, local NGOs and eyewitnesses interviewed by the Inspector have reported incidents of invasions of protected areas. Management corroborates several widespread invasions:

“One of the CUs [Conservation Units], the Candeias State Park (covering about 9,000 ha.) has been degraded and is being substituted by an expansion (of more than 55,000 ha.) of the Samuel Ecological Station.”

“[M]ost of the [State Forest Reserves] to be maintained under the Project present serious land tenure problems as they were created either on private land or have been *seriously invaded and are currently highly degraded.*”
[Emphasis added]

¹ For a discussion of the nature - shortcomings - of this Agreement see below at Box 4, para. 62.

“INCRA is taking steps to resettle some 97 squatter families living on the demarcated reserves of Uru-eu-wau-wau and Mequens.” (“Draft Report” Annex A paras. 9, 18, 28).

Burning

17. The substantial increase in fires in the Amazon, Rondonia in particular, has been widely reported at local, national and international levels. The indicator most utilized is the report of the Brazilian Space Research Institute (INPE). Based on weather satellites information 39,000 fires in July 1995 alone are reported, five times the number of July 1994. According to this source there were record levels of set fires during the entire dry season of 1995. Other data seem to confirm this report. An article in VEJA—a respected Brazilian weekly publication—provides a compelling description of the level of burning and deforestation in the Amazon region and their undeniable consequences for the livelihood of its inhabitants. As an illustration, ANNEX C contains, *inter alia*, articles from the New York Times, Times Magazine, and VEJA. The burning, whether done to clear land for agricultural purposes (generally without legal permits) or to destroy forests in order to claim title to land, disrupt zoning and, damages the natural resource base—the resource PLANAFLORO was intended to conserve.

Impact of Activities

Deforestation

18. All the above four activities result in deforestation.

19. In the absence of the project, PLANAFLORO forecasted deforestation to be around 850,000 ha per year (SAR Annex 3). This figure is obviously exaggerated, given INPE’s estimate of cumulative deforestation in Rondonia since 1960 of 2,000,000 ha. A recent study by FAO (Forest Resources Assessment, 1990), on the other hand, estimates deforestation in Rondonia during the 1980s at 231,000 ha per year, equivalent to 1.1% of the total land area per year. Therefore the PLANAFLORO original forecast is off by a factor of four. Based on unrealistic data, Project actions were supposed to lower this rate to below 300,000 ha per year during the first three years, 200,000 ha in the fourth year and 100,000 ha in the fifth.

20. In the absence of yearly deforestation rates from satellite data which should have been, but have not been provided by the Project, it is necessary to rely on literature data to estimate deforestation rates from 1992-1995.

21. Deforestation rates for recent years have been estimated to range between 200,000 and 400,000 ha per year. Moreover, the problem appears to have

worsened considerably this year, in particular with respect to fires which more than double last year's figures (see para. 17 above).

22. **Satellite imagery.** This is now available and can be analyzed to provide statewide deforestation rates during the life of the project. Although statewide analysis of deforestation trends in Rondonia based on satellite imagery will not be available until early 1996, the trend is illustrated by analysis of the Uru-eu-wau-wau indigenous reserve, where in that one reserve alone, the deforested area rose from 2,700 ha to 15,500 ha between 1992 and 1995—almost a 600% increase. For further discussion see Box 3.

Losses through Deforestation

23. Estimates are required to assess losses and wasted resources. Deforestation eats away the State's *natural* capital and contributes to the loss of forest reserves. There are well established methods to calculate the loss of forest reserves and correct national income accounts to take into consideration the *depreciation of natural assets*. These methods rely on the calculation of different types of losses produced by deforestation, including loss of wood, soils, etc. The three boxes below contain: (1) a note on methodology; (2) an estimate of material damage by forest loss statewide; and (3) an estimate of material damage by forest loss in the Uru-eu-wau-wau reserve from 1992-1995. The estimates of damage are calculated from the value of wood alone.

Box 1

ESTIMATE OF MATERIAL DAMAGE THROUGH FOREST LOSS IN RONDONIA

Methodology

- As a first approximation, material damage is estimated on the basis of forest loss alone, measured by commercial values for wood. It does not include other values, such as water, fish, soils, or biological diversity which are also affected.
- Annex 3 of the SAR provides an estimate of the values lost by forest destruction in Rondonia. This estimate includes only the value of trees lost to "rational highgrading" a process where only the most commercially viable trees are removed from the forest. Therefore it does not include the value of the remaining wood (about 75 cubic meters), long term sustainable wood production, soils, water or biodiversity losses. Annex 3 of the SAR estimates that one hectare of forest yields about 80 cubic meters, out of which 5 cubic meters would be high quality commercial species with a value of \$50 cubic meters.
- The methodology utilized here is more comprehensive and was developed to correct national income accounts to take into consideration the depreciation of

natural assets and has been accepted by UNDP and the UN Statistical Office (see “Integrated Environmental and Economic Accounting”, United Nations, New York 1993 (Sales No. E. 93. XVII. 12)).

Box 2

ESTIMATE OF MATERIAL DAMAGE THROUGH FOREST LOSS STATEWIDE

- Cumulative forest loss in Rondonia has been estimated by INPE to be approximately 20,000 square km, equivalent to 2 million ha or 5 million acres. Annual deforestation has been estimated to range between 2,000 and 4,000 square km. For purposes of this preliminary calculation, the most conservative figure (2,000 square km, equivalent to 200,000 ha or 500,000 acres) will be used.
- Considering an average price for wood of about \$20-25 per cubic meter and a yield of 80 cubic meters, the material damage caused by loss of wood is in the order of \$1,600-2,000 per ha.
- Using the conservative estimate of \$1,600 as well as the conservative deforestation estimate of 200,000 ha/year, the annual loss of wood is in the order of \$320 million, while the cumulative loss reaches \$3.2 billion.
- If the Planaflo project had been able to reduce deforestation by 10%, the loss of value avoided is in the order of \$32 million/year. For each additional 10% reduction, an equivalent amount (\$32 million) of loss would have been avoided.

Box 3

ESTIMATE OF MATERIAL DAMAGE THROUGH FOREST LOSS IN THE URU-EU-WAU-WAU RESERVE

- In the specific case of the Uru-eu-wau-wau Reserve, the total area cleared based on 1992 satellite data was 27.22 square kilometers and this area increased to 153.93 square kilometers by 1995, according to the analysis performed by Institute for the Study of Earth, Oceans and Space of the University of New Hampshire. Therefore, the deforestation that took place in the Uru-eu-wau-wau Reserve between 1992-95 was 126.71 square kilometers, equivalent to 12,671 hectares
- The value of the wood lost or extracted, which in this case can be considered as a damage to the indigenous peoples is equivalent to the 12671 hectares multiplied by the low estimate of the value of the wood (\$1600/hectare). This

results in a loss of forest valued at over \$2 million dollars in the three-year period. The figure does not include the considerable damages caused by erosion, loss of biodiversity or other products that can be extracted from the forest in a sustainable way.

24. In addition to the resulting monetary losses illustrated with reference to one of the many tribes represented in the Request, additional major losses, of a social and environmental nature not calculated here could be verified through an investigation.

Loss of sustainable income

25. Estimation of the damage by loss of wood alone is not appropriate. It does not capture other indirect impacts on income. Rubber tappers and indigenous people live mostly in a subsistence economy, many of them at the marginal level.

26. Deforestation impacts these groups because it reduces the size of their reserves and destroys forest resources. It also forces them to devote time, which would otherwise be devoted to productive activities, to police, control and report deforestation to the authorities— many times with disappointing results. For example, rubber tappers interviewed by the Panel in the Rio Cautario extractive reserve claimed that they had to spend about 10% of their productive time in activities related to deforestation control and that this loss of time had a proportional impact on their income. Recent reports from the Rio Cautario area claim that since decreed in August 1995—and pending implementation and enforcement of the borders—one-third of their time is now being spent on surveillance (see para. 64 below). Considering that the average income was estimated at about \$100 per month per family, a loss of one-third of income further underlines the extent and materiality of immediate damage caused by delays.

27. Due to delays in establishment of the Rio Cautario reserve, its area had to be reduced because squatters settled there pending demarcation. The reduction of the reserve area has also resulted in the loss of income: the loss of sustainable cashew nut production of about 200 barrels per year, for which the community of about fifty families would obtain about \$3,000—again a considerable damage in relative terms.

28. De-facto Zoning Changes. These examples illustrate a typical problem which inevitably arises when restrictive agro-ecological zoning plans are publicly announced but planning and execution are not synchronized. In other words, achievement of the objectives of project such as PLANAFLOORO depended heavily on its timely execution. Otherwise, as has occurred before, there is a rush to occupy land or extract wood from targeted areas before it becomes prohibited. Therefore Staff's repeated acceptance of expanded time periods for implementation of critical components enabled the inevitable to continue.

Armed Conflicts

29. Illegal logging activities cause harm or threatened harm to both indigenous people and rubber tappers. Both groups face constant threats to their lives by loggers or the armed groups they hire to protect their illegal deforestation operations. Since many reserves were not legally declared or physically demarcated, the Forest Police have been, at best, reluctant to intervene: rubber tappers or indigenous people must deal with such threats themselves. Rubber tappers interviewed by the Inspector in the Rio Cautario extractive reserve highlighted the fact that they must continuously risk their lives patrolling their reserve in an attempt to control illegal logging operations. Both the rubber tappers and leaders of their statewide organizations informed the Panel that the situation in Rio Cautario prevails in most, if not all, of the extractive reserves throughout the State. A 1993 BTO and independent observers have confirmed these statements.

30. Another example, relating to isolated tribes is provided in the Aide-Mémoire of the October, 1995 Bank's mission to Rondonia. A contact group for isolated indigenous people, along with some members of the isolated groups, were chased away by armed loggers.

Health

31. The Requesters claim they have suffered material damage through lack of basic health delivery mechanisms in particular to indigenous people. This has been compounded by the fact that federal agencies withdrew their support for Amerindian health services since they were supposed to be funded by PLANAFLORO. Management, on the other hand, recognized that provision of health services was "precarious" and "intermittent" until mobile medical teams visited every indigenous reserve "*on a regular basis starting in February 1995.*" (Draft Report, Annex A, paras. 31 & 32). In August 1995, however, provision of only intermittent health services and many cases of malaria (35 in one month) were reported in one indigenous peoples reserve visited by the Panel. Others interviewed reported that statewide infant mortality due to malaria is unacceptably high. Although there are further indications of material damage, the Panel cannot assess its extent at this stage since no reliable data are currently available. Such data could only be obtained on the ground during an investigation.

Finding

32. This additional review conducted since September 12, 1995 confirms the Panel's initial finding that illegal burning, logging and encroachment in areas reserved for indigenous people and rubber tappers constitute a substantial material damage since these populations rely basically on the trees, flora and fauna of these areas to

survive as distinct groups and to carry out their economic activities. Avoidance of such damage was one of the main objectives of the Project which, as agreed in legal documents, is to “protect and enforce the borders of all Conservation Units, Indigenous Areas, public forests and extractive reserves, and control and prevent deforestation, wood transport and forest fires in Rondonia contrary to Brazilian laws and regulations.”²

Bank Policies & Procedures

33. The Panel’s task is to establish whether the design and/or implementation of the project has been consistent with Bank policies and procedures; and if not, whether the Bank—through its actions or omissions— has contributed to the harm suffered by affected parties and if so, whether it has failed to remedy the situation.

34. The Requesters claim that the Bank violated a number of its own policies and procedures in relation to the design and implementation of the Project. The adverse effects of such violations were compounded, according to the Requesters, by the inability or unwillingness of the Bank to follow up on the obligations of the Federal and State Governments under the loan and project agreements.

35. The Management Response acknowledged delays in the project and cited a number of implementation problems. Indeed, supervision missions constantly rated project implementation as “unsatisfactory” without apparently triggering any urgent measures to enforce applicable loan covenants. Instead, the problem was dealt with by repeated informal revision of deadlines.

36. After a review of the Request and Management Response, the Panel reached the preliminary conclusion that, as explained in its Recommendation to the Executive Directors, there appeared to be several possible Bank violations of its own policies and procedures that may be linked to the material harm alleged in the Request. This expanded review requested by the Executive Directors, further substantiates the Panel’s preliminary conclusions. What follows is a brief discussion of the main areas where such violations may have occurred.

Design

LESSONS OF EXPERIENCE (OMS 2.12 AND OD 13.40)

² Loan Agreement, Schedule 2.

37. According to the Operational Directive (“OD”) 13.60, “one of the central ways in which the Bank improves its performance is by utilizing the findings of the Operations Evaluation Department (“OED”). The failed POLONOROESTE program³ was extensively reviewed by OED in a special Report No. 10039 (“OED Report”). It comprehensively chronicled and analyzed implementation failures of the social and environmental components of the program. Based on this the OED Report spelled out what the Bank needed to do to design and implement any follow-on projects in Rondonia. The SAR should have provided a complete accounting of how the follow-up Project, PLANAFLORO, had taken into consideration the OED Report’s “key findings and recommendations.”

38. It is worth noting that, while not circulated to the Executive Directors until April 1992—two months after approval of the PLANAFLORO loan—the OED Report was initially circulated for comment in 1990. Therefore, in addition to the Region’s Project Completion Reports (“PCR”), lessons of experience were available to Staff and Management during the design and appraisal of PLANAFLORO. A summary of a relevant part of the OED Report is attached as ANNEX D.

39. Fundamental problems in implementation essentially resulted from design failures which did not adequately take into account the lessons of the POLONOROESTE experience. Although the Staff Appraisal Report (“SAR” pp. 13-14) cites the “main lessons” learned from implementing agricultural projects under the POLONOROESTE program, the Project design and SAR failed, in reality, to draw upon the environmental and supervisory lessons. As a result, the Panel considers that the Bank failed to anticipate most of the existing major implementation problems at the design phase.

Institutional Capacity Building (OMS 2.12)

40. The Bank’s policy is categorical with regard to the importance of the project institutions, noting the centrality of “the relationship between institutional and output objectives so that the institutional and physical components can be made mutually supporting and the priority and strategy of institutional efforts clarified.”⁴ The policy further identifies a key issue in Rondonia: “knowledge of local traditions and attitudes is likewise essential in the design of workable institutional arrangements.”⁵

³ The POLONOROESTE program was launched by the President of Brazil on May 27, 1981, and was carried out with primary external financial support from six separate loans from the Bank totaling US\$ 434.4 approved in 1981-1983. The primary objective was to pave the existing BR-364 highway from Cuiaba to Porto Velho, and to provide related investments for “harmonious socio-economic development” of the region. The last Bank loan (New Settlements Credit) was closed on March 31, 1992.

⁴ Paragraph 17 (b).

⁵ Paragraph 21(d).

41. **Lesson of Experience.** Staff also received invaluable advice FROM the OED Report, which stated that before embarking on any further work in Rondonia, the Bank must be satisfied that there are: “Sufficient legal, technical, institutional and, above all, enforcement capabilities to adequately anticipate, monitor and control the direct and indirect adverse environmental impacts of on-going development processes at the local, state, and/or regional levels.” The OED was deeply concerned about this issue, and went on to say, “An obvious lesson for the future is the need to give particular attention to the judicious selection of the coordinating agency, as well as to the design of inter-institutional and implementing arrangements, in programs of similar complexity. More generally, this implies the need for the Bank to give much greater attention to institutional analysis and assessment during project appraisal and to institutional strengthening and development in project design and supervision.”⁶

42. Sufficient institutional capacity building to handle the ambitious, complicated PLANAFLORO program was not incorporated in the design phase. High standards, tight timetables/deadlines, and multiple tasks spread among a large number of State level implementing agencies were built into the program. In view of past experience, the Bank’s expectations of the borrower were unrealistic given the then existing or foreseeable capacity for implementation. Basic implementation problems and delays stem from this fundamental flaw in the design of the institutional infrastructure.

Agro-Ecological Zoning: Demarcation and Enforcement (OPN 11.02)

43. Bank policy on Wildlands requires protection of remaining natural habitats, especially when the areas are coterminous with indigenous populations whose social and cultural traditions are respected. The Amazon has long been identified as a priority area by the Bank for this approach.⁷ The directive in Annex III of Operational Note (“OPN”) 11.02 is highly relevant to the issues that arose in design and in implementation of PLANAFLORO -- “Implementation of important wildland components should, as a general principle, be well underway before a project’s major land clearing or construction works are allowed to proceed.” The infrastructure component of the PLANAFLORO Project includes rehabilitation of 3,900 kms of state and municipal roads and pavement of 81 kms, as well as other transport and maintenance activities—utilizing about a quarter of the total Project financing. In Rondonia there has always been a central tension between the need to demarcate and support reserves and the popular demand for more construction and rehabilitation of roads and other infrastructure.

⁶ p. 250.

⁷ OPN 11.02, Annex II.

44. For that reason, the PLANAFLORO project was designed to address, as a stated priority, the inappropriate exploitation of fragile areas due to absence of zoning and land use controls by providing a conceptual and institutional framework to introduce agro-ecological zoning based on a map more precise than the one produced by the POLONOROESTE project at a scale of 1:1,000,000 which was the “first approximation” to agro-ecological zoning.

45. PLANAFLORO’s implementation of agro-ecological zoning depended on the existence of detailed zoning and soil maps at a scale of 1:500,000 in Zone 1, (1.) 1:100,000 in Zone 1 (1.2), 1:250,000 in Zone 1 (1.3 and 1.4) and 1:500,000 in Zones 4, 5 and 6. *These maps were essential for the so-called “second approximation”, which was to be the basis for all legal demarcation of reserved areas and their enforcement, according to the SAR (para. 3.12) which states:*

“The available maps of Rondonia are at a scale of 1:1,000,000, except for a soil map of 1:500,000. While these have been adequate for general planning purposes, smaller scale maps are now needed for detailed planning and implementation (e.g., for proper border control of zones and reserves; agro-forestry planning for specific areas within Zone 1 and 2). The project would finance the preparation and distribution by ITERON of statewide agro-ecological, climatological, soil and topographical maps. During negotiations, the State of Rondonia provided assurances that these statewide maps, all satisfactory to the Bank, would be completed no later than December 31, 1993 and subsequently distributed (para. 4.01 (b)).”

“The project would also support the cartographic work necessary for the creation, management and protection of conservation units, public forests, extractive reserves and Amerindian reserves, and the border demarcation of approximately 9,900 kms and re-demarcation of another 1, 600 kms...” (para. 3.13).

It is not clear why the Management Response characterized the second approximation as mere “initial refinements” of existing statewide maps (Response 3.48).

46. **Lesson of Experience.** A basic recommendation of the OED Report was that much better and more extensive data gathering had to occur *before* launching follow-on efforts, with particular criticism leveled at the state of knowledge about agro-ecological and socio-economic realities in Rondonia. According to OMS 2.12, “it is essential to prepare the project *as far as possible* in light of the available information, to specify clearly the project objectives and ensure the commitment of

the Borrower (and the beneficiaries) to them, and to outline in some detail the essential inputs and arrangements with respect to organization, institutions and procedures that are expected to be necessary for achieving the objectives.”⁸ If, as acknowledged by Management, the second approximation was crucial to the project-- it should have been included in the design phase of the project or made a condition of loan effectiveness. As in the case of POLONOROESTE, the Bank again failed at the design stage to ensure that the protection of natural habitats and the homes of indigenous people would have the highest priority. Instead, the requirement for the contracting and completion of the second approximation was included as a dated obligation in the Project Agreement (Sec. 2.04), due to be completed early—no later than December 31, 1993. As discussed below at para. 62, *nearly two years later, the Draft Report indicates that the contract for this fundamental component of the project has still not been signed.*

Amerindian Component (OMS 2.34)

47. The design of the Amerindian component appears to have complied with much of Operational Manual Statement (“OMS”) 2.34 except for the central problem that no forum was created for direct participation of Amerindians in the project planning, design and implementation.

48. Management failed to take adequately into account the well known coordination problems among key agencies in Rondonia (FUNAI, ITERON, INCRA and SEDAM), despite OED’s explicit warning that no single agency was able to carry the institutional burden of programming to the Amerindian populations.

49. **Lesson of Experience.** One important lesson from POLONOROESTE was that demarcation alone was not enough:

“The physical demarcation of environmental conservation units and Amerindian reserves is a necessary, but not sufficient, condition for their protection. Financial disincentives, such as the absence of public physical and social infrastructure in the surrounding areas and strong enforcement capacity to prevent and punish invasions are also required for ensuring the protection of such areas.”⁹

⁸ Paragraph 31, emphasis added.

⁹ OED, p.114, quoting “lessons” from the Project Completion Report.

Project Implementation

GENERAL OBSERVATIONS

Institutional Capacity

50. The particular weaknesses of state environmental institutions were recognized in the 1994 Management “Status of Implementation Report” for the Executive Directors. Paragraph 60 Annex A of the Draft Report recognizes that co-ordination of Project activities has been weak and that fragility of key implementing agencies has been detrimental to Project execution (see also para. 52 below). In terms of strengthening State institutional capabilities, the Report shows that after almost three years there remains weak co-ordination among State and Federal agencies and ambitious state-wide execution plans are now mostly restricted to 15 “priority” municipalities (Draft Report, Annex A. para 63).

Infrastructure Expenditures

51. An objective of the Project was to remedy the adverse effects of implementation of infrastructure components of the POLONOROESTE program. The OED Report documents the adverse effects of an imbalance between expenditures for the infrastructure and environmental components. Under this Project the imbalance, as noted by the Staff, continues. A recent supervision mission pointed out that over half of the 1995 program expenditures have been on infrastructure, and that a redress of that imbalance would allow greater emphasis on the credit component.

52. At the end of 1992 Staff predicted there would be delays in the environmental component due to the underdeveloped nature of implementing institutions. To this end, a BTO memorandum (which also dealt with a related project in Mato Grosso), suggested that disbursements on infrastructure should be tied to progress in implementing the environmental components after observing as follows:

“In both states institutions responsible for implementing the environmental components are extremely weak. The elements of the environmental components and the steps necessary to implement them were not understood at the implementation level in either state.

In both states implementing agencies attribute problems of preparation to a high Staff turnover (poor wages and morale), the long delays in project preparation, changes in Bank personnel (lack of continuity) during Bank

preparation, and limited access to project documentation at the implementation level.

Significantly, infrastructure components of the projects do not suffer from the same delay-causing preparation problems.

Given the relative preparation of environmental and infrastructure components of the projects (in an all-too-familiar scenario) the Bank will retain little leverage (disbursements) by the time the states are required to show their commitment to the environmental components.”
[Emphasis added]

53. The April 1995 supervision mission acknowledged the potentially damaging environmental impact of continuing road construction long recognized to have adverse environmental effects. The letter sent to ratify the findings of the mission indicates how difficult it was to stop construction of a road even though it was three years after the beginning of PLANAFLORO:

“We would also like to highlight your personal commitment to ensure that the construction of the highway BR-421 will be discontinued as it contradicts the recommendations of the first approximation of the agro-ecological socio-economic zoning *and threatens the integrity of indigenous and extractive reserves and conservation units.*” [Emphasis added]

Project Administration

Supervision (OD 13.05)

54. Despite design failures Management should have identified implementation problems and moved expeditiously to solve them—through adequate supervision and monitoring. Failure to enforce loan obligations in violation of policies and procedures has undoubtedly contributed to the above- noted material damage.

Suspension of Disbursements (OD 13.40)

55. **Lesson of Experience.** History repeats itself in Rondonia’s treatment of the indigenous people. In the POLONOROESTE program, major problems were addressed only after major external protests and the completion of the mid-term review in early 1985. Some progress was made on the Amerindian component of POLONOROESTE *after* the Bank finally suspended disbursements in March 1985--the first time ever on environmental and social grounds. Funding was resumed in August 1985 after federal authorities moved to protect several vulnerable Amerindian areas and agreement was reached on an agenda for redirecting the program.

56. OED recommended early use of this remedy to ensure compliance in any future project of this type in Rondonia. The records examined by the Panel show that suspension of disbursements was never considered for PLANAFLORO until after the Request for Inspection was filed with the Panel.

Supervision (OD 13.05); Monitoring and Evaluation (OD 10.70)

57. PLANAFLORO was needed because the social and environmental components of POLONOROESTE were neither adequate nor implemented. Yet to date very little of what was planned under PLANAFLORO has materialized. Year after year, as in POLONOROESTE, new target dates were set for completion of various actions. Had the Bank insisted on the timetable set out in the Project documents, intended beneficiaries and their environment would have been better rather than worse off.

Delays and lack of enforcement

58. A review of selected Aide-Mémoire from November 1992 through October 1995 shows how deadlines set for implementation of various tasks were repeatedly unmet. The solution, in some cases still continuing, was to agree to another deadline in the next supervision mission's Aide-Mémoire. In other cases dates for completion of activities were set but, based on a review of selected internal documents, there appears to have been no follow-up in many cases. In any event, the lack of commitment of both parties to such deadlines is evidenced by the fact that they neglected to update the specific deadlines set forth in the loan and project agreements. Indeed, as a result, through these repeated informal extensions their enforcement became increasingly unlikely. ANNEX E contains an illustrative table tracing this pattern in relation to the Second Approximation (mapping), Legal Establishment of Reserves and Physical Demarcation, Enforcement of Zoning, Project Beneficiary and NGO Participation in Project Execution, and the Amerindian Component.

Implementation and Supervision of Credit Component

59. Part B.3 of the Project described in Schedule 2 of the Loan Agreement lays out the requirements for the development of rural credit including, *inter alia*, formal establishment of a denominated in-kind credit system, administration of such a system by BERON, and gradual provision of such in-kind credit. The institutional weakness and strained financial condition of BERON was apparent from the outset, yet insufficient attention was given to the Credit component in the various Aide-Mémoire. The component appears to have been introduced very late: only a small portion of funding for agroforestry has been released so far. Lack of supervision and

proper auditing procedures cast serious doubts about the effectiveness and proper execution of this component.

Supervision of Accounting and Auditing

60. Section 4.01 of the Loan Agreement and section 3.01 of the Project Agreement lay out normal requirements for financial reporting, including maintenance of separate accounts and annual audits. After almost three years of Project execution, no appropriate accounting and audit reports have been received. A Bank expert noted a number of irregularities in the accounting of loan funds. In spite of this the Bank continues disbursing on the basis of statements of expenditure. Now the Bank appears to have agreed to a “quick fix” to pending audit reports (Annex B, Draft Report) The Panel is most concerned that the necessary remedies, should the auditors discover any misapplication of funds since 1993, may either be impossible to implement or damage the overall potential of the project.

Monitoring and Evaluation

61. The Bank did not succeed in making Project monitoring operational. The Independent Evaluation Committee (“IEC”), required under Project Agreement 2.08(a), submitted only a draft of its first annual report six months late, no final, and no other reports since. The IEC represented an innovative effort at joint monitoring involving the borrower, the Bank, and NGOs. It did not work out (Report, Annex A para. 31). Instead, the monitoring and evaluation work has been contracted out to a consulting firm.

SPECIFIC OBSERVATIONS

Land Tenure Regularization

62. **Illegal Settlements (INCRA).** The Management Response characterized INCRA as “a Federal entity whose commitment to Project goals both in word and deed is a *sine qua non* for success.” No new settlements were supposed to be created and no titling of lands undertaken in areas that do not have sustainable development potential as identified by the agro-ecological zoning. The fundamental importance of this was recognized by requiring existence of an Agreement between INCRA and the State—as condition of effectiveness of the Loan. The following notes the history and adverse effects acknowledged by Staff:

- Section 2.12(a) of the Project Agreement required Rondonia to “enter into an agreement with INCRA concerning land regularization policies and practices to be observed in the State, which shall be consistent with the objectives of sound forestry protection and management, on terms and conditions satisfactory to the Bank”. This requirement was made a condition of effectiveness (Loan Agreement, Section 6.01(b)).

- The Management Response and Draft Report assert that this condition of effectiveness was complied with in November 1992.
- An Agreement, apparently “satisfactory to the Bank” was signed in November 1992. However this Agreement, as correctly stated by the Requesters, did not cover land regularization activities by INCRA. Such activities, as recognized by Staff (see below) have resulted in material adverse effects for intended Project beneficiaries.
- A 1994 Aide-Mémoire indicates that neither the borrower nor Management believed that the appropriate agreement existed:

“The mission was not able to discuss with the Regional INCRA Staff the problems related to land regulation, *which are one of the main obstacles to the project’s outcome. It was noted that the **lack of an agreement between the State of Rondonia and INCRA** has inhibited resolution of the land problems in areas 4, 5 and 6, and consolidation of the land situation in zones 1 and 2. Although it was previously agreed with Bank missions to prepare and implement a detailed work plan to carry out these tasks, this was not done.”
[Emphasis added]*

- A letter sent to ratify the findings of the April 1995 supervision mission addresses the issue directly and indicates that the Bank may finally have been willing to exercising its remedies under the Loan Agreement:

“...the Bank is also highly concerned with the inter-institutional collaboration required *first*, to ensure an orderly occupation of land in Rondonia based on the socio-economic agro-ecological zoning and *second*, to create and maintain the conservation, extractive, and Indigenous reserves envisaged under the referenced project and stipulated in the Loan Agreement 3444-BR, signed between the Federal Govt. and the Bank on September 19, 1992. *To that end, and as I am sure you are aware, it is essential for INCRA to enter into an agreement with the State of Rondonia on the lines discussed in Brasilia, on April 10 and 11, 1995, among the mission, INCRA and the State Government. The Bank, as one of the contracting parties of the referenced Loan Agreement, needs to have a definition of INCRA’s ability and willingness to sign the agreement with the State to fulfill the obligations stipulated in Loan 3444-BR by a definite date. We have been informed by INCRA’s President that the institution is currently analyzing the text of the Loan Agreement before it signs the*

agreement with the State. We would like to take this opportunity to reiterate that if a satisfactory solution were not found in the course of this month, the Bank will have no alternative but to consider the exercise of its rights along the terms of the Loan Agreement.” [Emphases added]

- The need for an appropriate agreement with INCRA was so self-evident that the head of INCRA-Rondonia later informed the Inspector during his visit that before its signature INCRA’s participation in PLANAFLORO was mostly “*de-facto.*”
- The required Agreement was finally signed after the Request for Inspection was filed--on July 4, 1995. The signing of this Agreement prompted the head of INCRA-Rondonia to issue a set of instructions, long overdue, instructing regional offices to respect the zoning and other provisions of PLANAFLORO.

Second Approximation

63. As noted above, mapping of the entire State in greater detail through the second approximation was included in the legal documents as a dated obligation to be completed by December 31, 1993. That deadline was missed. In subsequent supervision missions, Staff asserted the growing importance of awarding the contract for mapping as soon as possible. It was not done at the time of the Request, and as noted in the Draft Report, has not yet been signed. Thus, there has been a violation of a major covenant for almost two years with significant adverse consequences for the protection of the areas where the Requesters live and work.

Legal Establishment of Reserves and Physical Demarcation

64. Part B6 of the Project and provisions of the Loan and Project Agreements provide for the redemarcation, protection and maintenance of conservation units and indigenous areas. The table in ANNEX E indicates that the list of areas to be redemarcated is repeated year after year. Redemarcation of the Uru-eu-wau-wau reservation, for example, is a repeated priority in all three 1995 Aide-Mémoire. However, whether this will be achieved in 1995 remains uncertain.

65. The establishment of extractive reserves called for under the Project has been even more delayed. Early monitoring revealed that planned extractive reserves had been so damaged by unmanaged logging that it would not be worthwhile establishing them as reserves.

Enforcement of Zoning

66. Part A of the Project, entitled “Environmental Conservation, Management and Enforcement” calls for safeguard and protection of indigenous areas and

conservation units, as well as construction of civil works and infrastructure to make enforcement possible. Continuous enforcement of zoning was supposed to be carried out by all agencies including INCRA, ITERON, IBAMA and SEDAM.

67. **Monitoring of Compliance with Zoning.** Numerous violations of zoning have been documented with respect to the first approximation and they include INCRA settlements in zones 4, 5, and 6, reduction in the size of protected areas and extractive reserves, and illegal deforestation. Where these shortcomings have been recognized, the response has been to defer the solution to area compensation mechanisms to be included in the second approximation. Since the initiation of the second approximation has been delayed considerably, effective compliance and monitoring of zoning have not been a priority. It is necessary to ascertain the specific level of effort that has been devoted to compliance with zoning as well as to establish a complete list of zoning violations.

68. One particularly difficult area has been control and monitoring of illegal deforestation, where efforts appear to have been lax due to inadequate resource allocation and lack of coordination between different institutions.

69. To evaluate the extent of deforestation monitoring it is necessary to evaluate the number of illegal deforestation claims vis-à-vis the number and distribution of control efforts, in particular in protected areas such as Amerindian reserves and extractive reserves.

70. Yearly satellite images were supposed to be utilized to monitor deforestation, new roads and new settlements. At the present time, no yearly deforestation studies have been completed using satellite imagery. Recently, 1994 was substituted as the year to be used as baseline data to measure project progress. This choice of year is disturbing, given the fact that the Loan was approved in March 1992. Since no baseline had been chosen prior to this, no deforestation rates have been calculated since 1992. Delays in project implementation clearly contributed to forest reserve losses that, as indicated in Box 2, could reach hundreds of millions of dollars over the life of the project.

Popular Participation: Involvement of NGOs --OD 14.70

71. The innovative PLANAFLORO design for participation of beneficiaries, both through the five regulatory commissions and the Independent Evaluation Committee, was a challenging task that should have received significant Staff support. It quickly became apparent, however, that some groups of beneficiaries were not represented by the NGOs. Relations between the NGO Forum and the borrower broke down in 1994, were patched up briefly by a Bank supervisory mission, and in the words of Bank Staff, “deteriorated again during the last months of 1994.” As of the last supervision mission, attempts were still underway to bring in

special consultants to re-establish trust among the borrower, the NGOs, and the Bank.

72. The Panel notes with concern that the Management proposal to bring into project management, private business organizations (Draft Report para. 11) may result in the inclusion of representatives of the parties behind illegal logging, burning and other anti-zoning activities. The less sophisticated and poor representatives of the Project intended beneficiaries could be outmaneuvered, lose their trust in the Bank and further distance themselves from the Project.

Amerindian Component (OMS 2.34; OD 4.20)

73. Part A.6 of the Project Agreement lists five major requirements for assistance to the Amerindians. Section 3.06 places particular emphasis on registration of the reserves, and provision of health care to all indigenous areas. In internal reports it is acknowledged that illegal logging in their reserves is still not under control. Furthermore, the Uru-eu-wau-wau reserve is still not fully registered. There is wide-spread recognition that this component is poorly managed, and has so far failed to attain its objectives. Provisional health measures, for example, are not sustainable without Bank financing of recurrent expenditures.

Remedial Measures

74. Since the Request was filed, Management has agreed to some measures to bring the project into compliance with policies and to enforce obligations under the legal agreements. The last three Bank missions looked at possible remedial measures and agreed, as in the past, on a chronology of specific actions. Now the past-due obligations in the legal documents are pushed even further into the future and as in the past, the timetable is not been realistic. Non-compliance continues. The October mission indicated that, given realities, a new approach to implementation might be needed.

75. The “Agreed Plan of Action” presented in Annex D of the Draft Report pushes forward dates of compliance through actions and plans to be defined and agreed upon in the near/medium future, rather than an attempt to restructure the Project around a comprehensive and realistic assessment of available remedies and attainable objectives. To do so would necessarily entail taking into account OED lessons of experience and the past flaws and shortcomings of PLANAFLORO.

76. An open and fruitful discussion with Management and Staff took place during a meeting on December 4, 1995. The agreed remedial measures contained in the Plan attached to the Draft Report were explained. Panel members took the opportunity to express their underlying concerns, in particular with the proposed time-frame for the final definition and execution of the Plan.

The Panel would like to thank Management and Staff for all additional information they provided and for the frank, realistic assessment of the status of the Project at this point in time.

Findings

- Although originally conceived in part to address adverse effects of earlier projects, lessons from the shortcomings of the POLONOROESTE program were too often ignored in the preparation, design and implementation of PLANAFLORO. Therefore, similar problems have occurred that threaten to perpetuate social and environmental damage.
- Failure of the project's design to take into account the borrower's limited institutional capacity is forcing a belated focus on a limited set of achievable priorities.
- Critical delays occurred for three years between approval of the Loan and filing of the Request because:
 - The Bank did not supervise PLANAFLORO effectively and failed to enforce implementation of key actions that were to be the basis of successful execution of the Project.
 - Supervision of implementation has been weak due to the lack of a permanent presence of Bank Staff in the project area and a rather complacent reaction to repeated defaults on covenants under the Loan.
 - Shortcomings in supervision are evidenced by the fact that long delayed actions have suddenly become possible since the Request was filed.
- Delays in the project have contributed to a breakdown of trust between NGOs and the Bank, making the direct involvement of civil society in any reorientation of the Project important. Some of the remedial measures proposed in the Report regarding NGO participation may, however, result in future alienation of intended Project beneficiaries.
- Postponement of a timely reorientation of the Project has substantially delayed achievement of many of PLANAFLORO's objectives and caused continuing damage to the interests of intended beneficiaries.
- Now the situation for many intended beneficiaries is by and large worse than two years ago.

Conclusion

77. This additional review further substantiates the materiality of the damages and establishes the link between such damages and deviations from Bank policies and procedures in the design, appraisal and implementation phases. There is also no evidence that the Bank considered a possible enforcement of the borrower's and the State's obligations under the loan documents, as provided in ODs 13.05 and 13.40. Such actions and omissions must, in the Panel's opinion, be regarded as contributing to the material losses suffered by the Requesters.

78. To establish a comprehensive inventory of material damage throughout all project areas, and to detail the link between such damage and specific policy deviations, would take about six months. Attached is a "Work Plan" which we would follow should the Executive Directors deem necessary the conduct of a full investigation.

December 8, 1995

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