



5.3 Implementing commitments in the Indonesian palm oil sector

PABLO PACHECO and HERU KOMARUDIN

Introduction

Private-sector commitments to zero deforestation are a major step forward, with great potential to foster more sustainable production and consumption. But the implementation of these commitments has to confront diverse challenges, such as the ambiguity in policy processes, the politics surrounding what is desirable, and the difficulty of regulating a largely informal economy.

Expansion of crop plantations in the tropics continues to cause numerous negative social and environmental impacts, and oil palm is the most significant of the crops concerned, especially in Indonesia. This is particularly challenging, considering the legacy from policies on resource distribution that are embedded within patronage systems and the less than transparent political and policy processes associated with the questionable origins of palm oil development in Indonesia. State policies in the name of economic growth and rural modernization supported the expansion of a sector concentrated in the hands of a few large-scale companies by using policy incentives and granting state forests for conversion. These contributed to the original capital accumulation in the palm oil sector, which also benefited from a declining timber industry that was exhausting natural forests (Casson 2000).

Companies committing to zero deforestation include those that have caused much deforestation in the past, including conversion of primary forests in Sumatra and Kalimantan, which triggered social conflict by ignoring customary tenure rights (Pirard et al. 2015). But due to pressure from consumers and civil society groups, they now have the opportunity to upgrade their corporate image (Gnych, Limberg and Paoli 2015).

Indonesian palm oil sector commitments to zero deforestation have been framed more broadly as “No Deforestation, No Peat, No Exploitation.” These pledges, therefore, address a more complex goal than just halting deforestation, by also committing to no



SOLVING THE OIL PALM
PUZZLE REQUIRES A
COLLABORATIVE
APPROACH.

Pablo Pacheco is Team Leader, Value Chains, Finance and Investments; and **Heru Komarudin** is a researcher. They both work for CIFOR, Bogor, Indonesia.

more plantations in peatlands, protecting local community rights, and stimulating greater social inclusion in the supply chain.

A controversial crop with contrasting impacts

Official statistics report that after rapid expansion, there were 11 million ha of oil palm plantations in Indonesia in 2015. This has been accompanied by fervent controversy, due to the contradictory social and environmental impacts of this controversial crop (Sayer et al. 2012). Production is dominated by large-scale companies, but involves an ever larger number of smallholders, who contributed to an estimated 40% of total planted area in 2014 (Directorate General of Estates 2014). The palm oil industry generates significant earnings for the government and stimulates economic growth in rural areas, with spillover effects on the development of infrastructure and support to rural livelihoods (Edwards 2015). But large-scale plantation development has also been implicated in numerous social conflicts, and the unequal distribution of benefits remains an issue (Colchester and Chao 2013).

The crop's greatest offence is that oil palm expansion often occurs at the expense of primary and secondary forests and peatlands, and is amplified by the use of uncontrolled fire during clearance (Tacconi 2016). The result is a major loss of biodiversity and increased greenhouse gas (GHG) emissions, which certainly raises questions about when, if ever, palm oil can qualify as "carbon neutral" (Khasanah et al. 2015). The Government of Indonesia estimates that deforestation and fires account for 63% of the country's GHG emissions (Government of Indonesia 2015), but others suggest that this could be as high as 80%.

The Indonesian palm oil sector

Major corporate groups — including Musim Mas, Wilmar, Golden Agri Resources, Asian Agri and Sime Darby — have embraced the concept of sustainable palm oil production, mainly by adhering the Roundtable on Sustainable Palm Oil (RSPO). This certification system has seen a slow but steady increase in uptake. About 21% of total global supply is now RSPO certified (RSPO 2016); this includes many older and less problematic concessions, which may limit prospects for further uptake. In addition, in order to export to biodiesel markets under the European Union's Renewable Energy Directive, producers have to obtain International Sustainability and Carbon Certification. Also, plantations are supposed to comply with Indonesian Sustainable Palm Oil (ISPO) standards, which are mandatory. ISPO was established in 2011 and based on existing Indonesian legislation, and its uptake is also slow. This has forced the original deadline for compliance to be postponed.

However, increasing pressure from civil society groups, through attacks on corporate brands and reputations, led several major consumer goods manufacturers to go above and beyond these standards and pledge to completely delink their supply chains from deforestation. Momentum began in 2010 when the Consumer Goods Forum and its

members committed to zero net deforestation by 2020. This was followed by individual and collective pledges, notably the Sustainable Palm Oil Manifesto (SPOM), the Indonesia Palm Oil Pledge (IPOP), and, in late 2014, the New York Declaration on Forests.

These private-sector commitments relied heavily on the concept of high conservation value (HCV) areas, which was already embraced by RSPO. However, there was no agreement on a definition of forests or on a methodology for designating “go” and “no-go” areas. The Steering Group of the NGO-driven High Carbon Stock (HCS) approach developed a toolkit to inform companies about suitable zero-deforestation practices, and HCS Plus, driven by the private sector, commissioned a high carbon stock study linked to SPOM. Both groups arrived at different carbon thresholds to define HCS forests, and gave different guidance on what rules to follow, but the two definitions and methodologies were aligned in late 2016.



By December 2016, 269 companies in the world had made commitments to support sustainable supply in the palm oil sector, mainly consumer goods companies,

retailers, traders and processors. Of these, 114 included zero-deforestation commitments (Forest Trends 2016), but these have yet to be fully embraced by their third-party suppliers, which are often controlled by Indonesian groups, or by a large number of smallholders.

Implementation challenges

Legal barriers and government opposition

The legality of current practices is the major constraint to implementing commitments to zero deforestation and/or achieving RSPO certification. Current laws still allow areas to be cleared for plantations if they are classified as convertible production forests whose definition is not based entirely on carbon stocks. Companies keen to set aside areas for conservation or carbon values within their concessions find that these areas are not fully recognized by Indonesian law or ISPO. Only parts of HCVs, such as riparian or threatened habitat, are recognized. However, the recently established multi-stakeholder task force to strengthen the ISPO has endorsed the legalization of a broad concept of HCVs for potential inclusion into ISPO principles and criteria, and has adopted sustainability principles endorsed by the Council of Palm Oil Producer Countries.

In 2014 the five most influential palm oil corporate groups in the country signed the Indonesia Palm Oil Pledge (IPOP) and established a secretariat to implement their commitments. The pledge aimed to harmonize commitments with existing regulations, embracing a comprehensive agenda for enhancing traceability, improving the image of Indonesian palm oil, and supporting smallholder inclusion. This broad agenda surpassed the capacity of IPOP, however, and intruded on the role of the national government, who

strongly opposed the pledge, branding it a cartel that violated competition laws. The government also argued that IPOP's zero-deforestation commitments actively excluded smallholders and SMEs from global markets. IPOP was disbanded in June 2016 after a tense relationship with the government, which eventually imposed state views on oil palm over those of private corporations.

In addition, the government chose to prioritize peatland restoration and fire prevention, and new regulations outlaw oil palm plantations on burned areas in addition to the existing moratorium on primary forests and peatlands. However, the government is also working on a law to protect the economic importance of oil palm, which makes its commitments somewhat ambiguous.

Moral and economic dilemmas

Zero-deforestation commitments have exposed two dilemmas. The first is moral, with the desirable goal of halting deforestation a possible constraint to maintaining or increasing smallholder livelihood opportunities from oil palm production. The second is economic: preventing the negative environmental impacts of oil palm expansion while not jeopardizing the potential to support economic growth and poverty reduction.

The social exclusion argument was used to oppose zero-deforestation, arguing that it would exclude smallholders from supply chains controlled by the companies that embrace such commitments and reduce the opportunities for oil palm to contribute to rural poverty alleviation goals. A complementary discussion was how to reduce the significant yield differences between smallholders and company plantation; although some companies are making progress, they are not fully supported by government actions.

In July 2015 the Indonesian government launched the Crude Palm Oil (CPO) fund. Fed by a levy on palm oil exports, the fund is used to subsidize biodiesel production and support intensification of smallholder oil palm production. The government claims that this has resulted in reduced GHG emissions and has cut the country's dependency on fossil fuel, but it is unclear how this is linked to goals associated with avoided or reduced deforestation in oil palm plantations. In addition, very little of the CPO fund has actually been distributed to smallholder farmers so far, being constrained by their unclear legal tenure. Current policies are not effectively linked to incentive policies, and it remains unclear how the issue of tenure rights will be resolved.

Regulating informal relations

Major corporate groups have made considerable progress in the traceability of supplies from mills to refineries, and from plantations to mills, but more work is needed to put systems in place that trace supplies from independent mills. These mills purchase from



an extended network of intermediaries, who in turn source from many tens, hundreds or thousands of small smallholders, often through informal relations.

Implementation of zero-deforestation commitments has made evident the clash between the formal industrial palm oil sector and the large informal smallholder economy. Tenure and finance are strongly shaped by informal local transactions. For example, in many



cases, local elites with access to political power benefit from allocating land permits or from stimulating informal and speculative land transactions fuelled by oil palm expansion. Many smallholders have no formal access to land, and lack clear rights when they illegally encroach on state forests. They make use of informal financing from local banks via intermediaries, and the state has proven that it is unable to regulate the informal economy.

The persistence of the informal economy creates significant challenges for corporations that attempt to implement traceability systems involving independent smallholders. Smallholders lack formal claims to land and cannot access public funding and incentives, which hinders compliance with sustainability standards, threatening to further alienate smallholders from the formal (sustainable) economy.

Potential and risks

Zero-deforestation commitments create an important incentive to invest in more efficient use of inputs, intensification, and improvements in plantation environmental management. These commitments may also include upgrading smallholder production systems, and expanding plantation development into degraded or low-carbon land, which helps to meet national emission reduction targets under Indonesia's Intended Nationally Determined Contribution.

Intrusion of large-scale producers into communally- or smallholder-owned degraded land also carries risks, as it could lead to increased social conflicts. But the main risk is excluding smallholders who cannot meet, or report on, stringent zero-deforestation standards because of unresolved legal issues and capacity constraints. This would result in fragmentation into "green" (clean) and "brown" (dirty) supply chains, and prompt leakage as suppliers might target less demanding markets. Of primary concern to the national and regional government — along with many local governments — is the potential risk of slowing development, since so much hope for rural economic growth is associated with the development of plantations, of which oil palm is currently the preferred choice.

Conclusions

Overcoming the challenges that face the future of zero-deforestation requires harmonizing perspectives from the private and public sectors to navigate the politics around the moral and economic dilemmas, and tackling the deep roots of the informal economy. Commitments to achieving deforestation-free supply chains have the potential to improve the smallholder supply base while reducing pressure on forests and peatlands, but only if they are synchronized with state actions and are complemented by policies that penalize illegal expansion on forests and peatlands.

The government's main issue is how to regulate the industry so that it supports smallholder and medium-scale producers under credible and enforceable national governance standards. Furthermore, it needs to do so while also reducing yield gaps, given the lack of access to capital and training, and while increasing human resources to enforce such standards. At the same time, the government must maintain its competitive edge in international markets, part of which is related to the credibility of mandatory standards, so that the industry can continue to contribute to national fiscal earnings and associated economic spillover benefits.

The private sector must continue to respond to pressure from civil society and buyer demands if it is to maintain its market share, but it must do so in a way that doesn't risk losing third-party suppliers. Businesses can do this while making a profit, finding investments to upgrade their value chains, and improving production efficiency and supply chain design and management. But, ultimately, they must protect their position in the market without risking any chance to expand their plantations. Third-party suppliers and smallholders also face multiple challenges, many of which they are unprepared for.

Solving the oil palm puzzle requires a collaborative approach that brings together public and private initiatives. Neither public regulation nor private commitments should dictate the rules of the game. The private sector must do what it does best — invest and innovate to improve efficiency and increase profits — while the government must look to protect wider national interests and natural capital.

In summary, five points are important:

- Oil palm is a controversial crop due to contradictory impacts associated with its expansion.
- Zero-deforestation pledges were easily embraced, but with little clarity on implementation.
- Strong political disputes on which rules to follow have added confusion to the process.
- Several challenges make it difficult to implement private-sector commitments.
- Overcoming obstacles requires collaboration between private- and public-sector actors.

References

- Casson, A. 2000. *The Hesitant Boom: Indonesia's oil palm sub-sector in an era of economic crisis and political change*. Bogor, Indonesia: CIFOR.
- Colchester, M. and S. Chao. 2013. *Conflict or Consent? The oil palm sector at a crossroads*. Forest Peoples Programme, Sawit Watch and TUK Indonesia, Moreton-in-Marsh, UK.
- Directorate General of Estates. 2014. *Tree Crop Estate Statistics of Indonesia 2012–2014: Oil Palm*. Jakarta, Indonesia: Ministry of Agriculture.
- Edwards, R. 2015. *Is Plantation Agriculture Good for the Poor? Evidence from Indonesia's palm oil expansion*. Canberra, Australia: Australian National University.
- Forest Trends. 2016. *Commitments That Count: Palm*. Washington, DC, USA: Supply Change, Forest Trends.
- Gnych, S.M., G. Limberg and G. Paoli. 2015. *Risky Business: Motivating uptake and implementation of sustainability standards in the Indonesian palm oil sector*. Bogor, Indonesia: CIFOR.
- Government of Indonesia. 2015. Intended nationally determined contribution. Jakarta, Indonesia: Government of Indonesia.
- Khasanah, N., M. van Noordwijk, H. Ningsih and S. Rahayu. 2015. "Carbon neutral? No change in mineral soil carbon stock under oil palm plantations derived from forest or non-forest in Indonesia." *Agriculture Ecosystems & Environment* 211: 195–206.
- Pirard, R., A. Fishman, S. Gnych, K. Obidzinski and P. Pacheco. 2015. *Deforestation-free Commitments: The challenge of implementation. An application to Indonesia*. Bogor, Indonesia: CIFOR.
- RSPO (Roundtable on Sustainable Palm Oil). 2016. *RSPO Impacts*. Kuala Lumpur, Malaysia: Roundtable on Sustainable Palm Oil.
- Sayer, J., J. Ghazoul, P. Nelson and A.K. Boedhihartono. 2012. "Oil palm expansion transforms tropical landscapes and livelihoods." *Global Food Security* 1: 114–119.
- Tacconi, L. 2016. "Preventing fires and haze in Southeast Asia." *Nature Climate Change* 6: 640–643.