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## DRIVING SUSTAINABILITY IN INDONESIA'S PALM OIL SECTOR The Role of the Indonesian Government's Certification System: ISPO

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### EXECUTIVE SUMMARY

Palm oil producers and exporters globally have responded to concerns about palm oil's environmental issues and social impact by encouraging voluntary certification systems. Besides that, the new mandatory government-backed certification system gives a clear assurance of legality and sustainability of palm oil agriculture and its derived products across the whole country.

Indonesia has determined to adopt and pursue the government-backed certification scheme, namely Indonesia Sustainable Palm Oil (ISPO). The ISPO emerged in 2011, while its standard and subsequent revision process commenced in 2016, have been critical for Indonesia. It has served three key purposes for Indonesia palm oil, aligned with the objectives of President Joko Widodo, such as (i) to improve the management practices and standards of the Indonesian palm oil sector including smallholders; (ii) to improve the acceptability and competitiveness of Indonesian palm oil in international markets; and (iii) to reduce Indonesia's greenhouse gas emissions.

### Background

Palm oil has become the world's fastest-growing oil crop, fulfilling global demand across industry sectors from food ingredients, cosmetics, and renewable energy. Moreover, as the most land-efficient oilseed crop, palm oil also ensures more land is free for forest conservation and wildlife protection even as demand grows along with global population growth.

### RECOMMENDATIONS

1. Along with the regional government, palm oil communities, and other stakeholders related, the government of Indonesia should continue developing the ISPO system to bond its position as a global leader in sustainability standards.
2. The government of Indonesia should engage with Indonesia's trading partners and development assistance partners to examine synergies between ISPO and development assistance programs relating to poverty reduction, agricultural productivity, and the environment/ climate issues.
3. Encourage Indonesia's trading partners and donor partners to consider opportunities to incorporate ISPO and related sustainability initiatives as part of the current and prospective collaboration mechanism.

However, the palm oil sector continues to face examination from anti-palm oil activists claiming negative environmental and social impacts associated with palm oil production where generally emerged from Western Europe. This has resulted in high demand from Europe for assurances of sustainability aspects for palm oil. As the largest global palm oil producer, Indonesia has initiated the government-backed certification system, namely Indonesia Sustainable Palm Oil (ISPO), to increase the global uptake of sustainable palm oil.

Currently, other certification schemes exist, such as International Sustainability & Carbon Certification (ISCC), Roundtable on Sustainable Palm Oil (RSPO), and Malaysian Sustainable Palm Oil (MSPO). In agricultural commodity markets, palm oil companies are leading the market transformation to reduce deforestation and greenhouse gas emissions through rapid certification and adoption of other voluntary sustainability standards. It is supported by CDP (2020)<sup>[1]</sup>, which assessed agriculture companies' deforestation commitments in seven commodities sectors and found that palm oil companies have the highest average number of firms reporting on production traceability, third-party certification, and stakeholder engagement. Furthermore, it is noted that European oilseeds such as rapeseed and sunflower – the direct competitors of palm oil in European marketplace – do not appear on the list of the most certified commodities.

## Benefits of Certification Systems

Certification systems have been introduced into global commodity markets to underline the sustainable production of commodities. Over recent decades, sustainable products have gained traction in mainstream consumer markets (mainly in Western countries). Consumers have increasingly become environmentally conscious, thus encouraging companies to disclose information and ensure sustainable practices along the supply chains.

From an economic perspective, certification systems provide legality and sustainability assurance to consumers. The system may offer purchasing options and address the consumer desire to purchase products guaranteed to be sustainable<sup>[2, 3]</sup>.

4. Indonesia's existing Free Trade Agreement (FTA) partners with specific sustainability requirements (for instance, European Free Trade Association) are suggested to undertake precise engagement with the government of Indonesia on pathways to recognizing ISPO.
5. Prospective FTA partners should recognize the ISPO and other national sustainability standards, also clearly understood and engaged throughout the negotiation process.
6. Specific sustainability regulations in consumer countries (for instance, the European Union Due Diligence regulations) should consider national certifications, particularly the ISPO.
7. Any Due Diligence regulations – and other similar efforts – should not consciously exclude the legality standards and national certification schemes. This would be a hostile act targeted to producing countries, in turn, to establish a form of regulatory imperialism from the west, which attempts to force Indonesian companies to give (for instance) the European Union regulations supremacy over Indonesia's laws.

For producers, government-backed certification systems have the potential to widen market opportunities, particularly for smallholders and independent farmers to gain access to mainstream markets and participate in global value chains. Additionally, certification systems can encourage producers and other supply chain actors to become certified by rewarding them with a premium price for sustainable products.

From an environmental perspective, certification systems and other voluntary sustainability standards lead producers to comply with criteria that minimise the adverse environmental and sustainable impacts, namely deforestation, biodiversity loss, and land clearing on peatlands<sup>[4, 5]</sup>.

In agricultural commodity markets, palm oil companies are leading market transformation in reducing deforestation and greenhouse gas emissions through rapid certification and adoption of other voluntary sustainability standards. Compared to other commodities, palm oil is the most certified commodity with a total of approximately 19%, followed by forestry (10.4%), soy (1.8%)<sup>[6]</sup>, and cattle<sup>[7]</sup>. European oilseeds such as rapeseed and sunflower, the direct competitors of palm oil in the European market, do not appear on the list of most certified commodities.

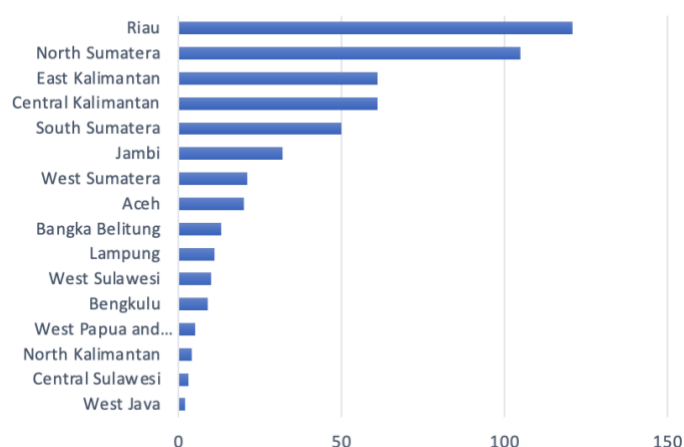
Despite the clear advantages of sustainability certification, requirements for certification pose some challenges for palm oil producers, particularly smallholder farmers. In Indonesia, 40% of the total palm oil plantation area is managed by smallholder farmers. However, uptake from voluntary schemes, most notably the RSPO, has been low among smallholders due to entry barriers and cost. Hence, the lower barriers to entry of the ISPO and different standards for smallholders manage to address this.

Increasing accessibility to certification systems for smallholders in Indonesia is important given the significant share of smallholders within the industry, and its implication on the supply of sustainable palm oil in the market.

## Potential Opportunities of ISPO: Pathway to International Recognition

The ISPO certification system is mandatory for palm oil plantations, whether from private-large companies, state-owned or cooperatives, plasma or independent smallholders. Since the inception of ISPO in 2011, approximately 621 oil palm plantations have been certified, covering about 5.45 million land hectares. The ISPO is also audited by an independent body for certification supervision called *Komite Akreditasi Nasional* (KAN), showing and assuring the system is run according to the best practice principles for certification.

### Distribution of ISPO Certificates by Region



Source: Directorate General of Plantations (2019)

The ISPO framework consists of seven principles, entailing three main themes: policy and legal; best management practice; and social, economic, and environmental perspectives. The principles and criteria (P&C) and implementing regulations of ISPO also aligned with existing legal and regulatory requirements, namely the Indonesian Environmental Feasibility Assessment (*AMDAL*). Since its commencement, the government of Indonesia has continued to strengthen the design and implementation regulations of the ISPO certification system by aligning with other certification systems and being recognised and accepted in the global market.

A comprehensive but straightforward analysis of ISPO against other palm oil certification systems demonstrates that the scope of ISPO in terms of its principles, criteria, and indicators is nearly identical to other existed systems. The ISPO also clearly has more significant levels of institutional support for smallholders. Importantly, the ISPO has specific provisions on labour that are unique and suit the Indonesian context.

However, there remains reluctance from several governments, particularly in Europe, to recognise the ISPO's significance within Indonesia. Unlike other certification systems, the ISPO has specifically oriented towards Indonesian sustainable development. Therefore, support for ISPO from other governments in Europe and abroad is vital. There are three markets where recognition opportunities are possible: the European Union (EU); EFTA countries, notably Switzerland; and the United Kingdom (UK).

The EU can potentially recognise ISPO through a bilateral trade agreement currently under negotiation with Indonesia. It can also recognise ISPO under its various sustainability measures within the Green Deal. This includes proposed due diligence regulation on preventing "imported deforestation".

EFTA countries, notably Switzerland, similarly have the opportunity to recognise ISPO under its free trade agreement with Indonesia (IE-CEPA), where certified sustainable palm oil is given preferential market access under the terms of the agreement.

The UK is currently introducing regulations that will prevent the importation of illegally produced commodities that may contribute to deforestation. However, the UK has chosen to use legality, rather than sustainability, as the test for this important requirement. ISPO, which has a legality requirement for production, will meet this requirement.

Relevant stakeholders, mainly the UK and the EU, should be open to accept and recognise the relevance of the national certification system and how the ISPO can contribute to achieving sustainable development goals in Indonesia.

## Conclusion

Palm oil is a strategic export commodity to national development as it contributes to generating export revenues, alleviating poverty in rural areas, and creating job opportunities. The government of Indonesia established the ISPO certification system, and so the continued development to strengthen national certification standards to achieve sustainable palm oil production in Indonesia must be acknowledged.

The international community needs to understand the importance of national certification systems. Recent international policy developments in the EU, notably the plan on phasing out palm oil for biofuels by 2030 and proposed due diligence requirements on deforestation and forest degradation, shows a lack of recognition and understanding.

Discriminatory trade measures will hinder the development of sustainable palm oil production and the development of producing countries. As studies have shown, banning palm oil from the global market would not be a sustainable solution given the high economic and environmental costs of substitution (rapeseed, soy, sunflower). Therefore, pushing for certified sustainable palm oil production in producing countries is fundamental. In the case of Indonesia, international recognition of the ISPO certification system is the most important element of proving that Indonesia is the leading producer of palm oil, and indeed any vegetable oil, globally.

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