

## How the EU Can Revise its Biofuel Policies to Promote “Sustainable” Palm Oil Cultivation in Southeast Asia

### Key Findings

- *The EU biofuels market stimulates rapid growth in oil palm plantations in Southeast Asia.* Europe’s already substantial imports of palm oils for food, detergents and cosmetics have been further boosted by demand for liquid biofuels, partly because palm oils replace other food oils diverted for energy consumption. Forthcoming revisions of the European Union’s Renewable Energy Directive (EU-RED) should take into account the impacts of this expansion.
- *Government legislation in producer countries is not sufficient to ensure sustainable production.* Palm-oil producing countries in Southeast Asia often have low capacity to enforce government legislation. For example, implementation of integrated management of river basins and catchments, and general environmental regulation, is often weak or non-existent.
- *The sustainability criteria in the EU-RED are insufficient to ensure responsible production.* The sustainability criteria are maladapted to the socio-ecological realities and production histories in local contexts in South East Asia. For instance, extensive conversion of peatlands took place prior to the 2008 baseline set in the EU-RED (and is still taking place).
- *Market-based sustainability standards accredited under the EU-RED differ radically in quality, and few include procedures to safeguard the rights of local communities.* Owing to the design of the EU-RED, few of the accredited standards include criteria on wider impacts on natural resources, livelihoods, and community rights. Given the technical and resource requirements associated with certification, smallholder farmers often struggle to obtain market access.
- *The EU ignores the precautionary principle embedded in international environmental law.* The EU is currently not responsive to the demonstrated impacts of palm oil production. This is reflected in the weak sustainability criteria in the EU-RED, as well as the fact that EU delegates responsibility for impacts to voluntary market standards.

### Background

The Renewable Energy Directive (2009/28/EC) (EU-RED) sets an EU-wide target which, by 2020, aims for 10% of the energy used in the transport sector to be generated from renewable sources.



Günther Oettinger, Member of the EC in charge of Energy, gives a press conference on the first EU sustainability schemes for biofuels in July, 2011

If biofuels used in the EU – whether produced locally or imported – are to be eligible for government support, or to count towards mandatory national renewable energy targets, they must comply with the so-called Sustainability Criteria. These are set out in articles 17, 18 and 19 of the EU-RED. EU demand for biofuels is a politically constructed (“premium”) market with particular tax subsidies and regulatory requirements. This merits special scrutiny of the effects of EU imports and the renewable energy policy framework.

The EU-RED places a dominant emphasis on GHG emissions, and makes no attempt to regulate for sustainable management of land and water resources in biofuel production outside the borders of the EU. It remains optional for member states to monitor such impacts. Nor does the EU-RED include social and/or economic criteria related to impacts on local livelihoods. The Sustainability Criteria only cover land use change, and, in the actual process of cultivation and production, disregard quality and quantity of water resources, local livelihoods and resource rights. This approach in the EU-RED is justified by reference to the free trade principles of the World Trade Organization (WTO) and to the risk of legal liability if the EU were found to promote protectionism. The approach reflects a specific interpretation of the long-standing controversy over whether customs unions, such as the EU, can prescribe standards that aim to regulate how imported products are produced.



Crude palm oil tanker inside a palm oil plantation in Borneo, Indonesia

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### The expansion of palm oil cultivation in Southeast Asia and its consequences

Palm oil, generally traded as Crude Palm Oil (CPO), is one potential source of biodiesel. However, the majority of imports of palm oil to Europe (which doubled in the period 2000–2006) is for the food industry, partly to replace rapeseed oil, which is increasingly used to produce biodiesel. Although the production of palm oil (and other crops that can deliver bioenergy feedstock) can help to meet domestic energy needs, lift some groups out of poverty and contribute to national economies in the South East Asia, the business also has a well documented traumatic legacy, particularly from large scale plantations, caused by unceasing expansion and resource degradation, marginalization of indigenous groups, and adverse impacts on communities that do not benefit.

Our research (see box) revealed that palm oil production has significant impacts on land and water use in all three cases studied. In Central Kalimantan in Indonesia, local communities, NGOs and government officials report that the expansion of oil palm plantations and establishment of palm oil mills have led to widespread pollution from toxins and organic matter, disappearance of fish stocks and aquatic wild plants, and drying of community land and village wells. In Thailand, palm oil plantations are encroaching on arable land held by small-holder farmers and compete with other crops such as rice. In Cambodia, an increasing number of land disputes and conflicts are reportedly connected to the allocation of land for large-scale palm oil plantations.

### Voluntary sustainability standards

The EU encourages national authorities, companies and NGOs in producer countries to implement certification schemes for biofuel production that comply with the sustainability criteria laid out in the EU-RED. These schemes are voluntary. In a Commission Implementing Decision of July 2011, the EU accredited seven certification schemes, and new schemes are continuously accredited. Schemes will not be accredited unless they meet technical requirements for how GHG emissions are calculated, following the spirit of the EU-RED as a climate change mitigation policy. This emphasis tends to promote more centralized schemes, while schemes that build on broader stakeholder participation and take into account a wider range of local impacts face more inertia in securing agreement. Furthermore, sustainability standards compete for buy-in from market actors, which means they must aim to please companies. Thus, such schemes cannot alone be expected to adequately represent the interests of local people in producer countries.

The standard of the Roundtable on Sustainable Palm Oil (RSPO) offers more robust protection for natural resources and livelihoods in producer countries than many of the accredited schemes. However, since it is not yet eligible for the tax exemptions in the EU market, it is difficult for the RSPO to offer a financial premium to its members. This means that buyers and retailers are less interested, leading to a limited supply-side response. The lack of financial incentives also means that certified members are less motivated to take seriously the



## About this research

SEI and its partners recognised that there is a lack of research into how the EU-RED drives land use change and natural resource use associated with the expansion of palm oil concessions in Southeast Asia, as well as into how governance systems respond to their impacts. To meet this need, we carried out case studies on the production of palm oil and other bioenergy crops in Central Kalimantan, Indonesia; Nakhon Si Thammarat, Thailand; and Sihanouk and Kampong Cham, Cambodia.

The palm oil sector differs markedly in each of the countries studied. In Indonesia, the majority of production is led by large-scale export-oriented corporate plantations. There is a legal requirement for companies to support smallholder farmers (on so-called “plasma” plots) but the implementation is not always effective. In Thailand, the government is promoting a rapid expansion of the oil palm sector. Its oil palm sector is dominated by smallholder farmers: 95% of the palm fruit sold to the 60 mills in the country is produced by 120,000 smallholders.

Thailand is ranked as the world’s third largest producer of CPO, and international demand for Thai-produced CPO is growing, including from the EU. This has led to concerns that there will be a lack of CPO for domestic use. In response the Thai government has introduced an export surcharge to encourage producers to sell oil on the domestic market. Cambodia has a fledgling oil palm industry, and does not yet have refineries to derive processed palm oil from CPO. In the absence of national strategies, expansion is taken place on an ad hoc basis.

RSPO principles and criteria (P&Cs). Several companies certified by RSPO have been criticized for non-compliance with both the RSPO standard and public sector regulations. Indeed, the RSPO has problems enforcing its own code of conduct and grievance procedure, and has not yet excluded any grower from its membership. However, EU support for the RSPO standard could considerably boost its effectiveness.

Auditing under the EU-RED relies on the “mass balance model” to monitor compliance with certification schemes. Economic providers in the audit trail must show that the share of the product certified reflects the share of the final product. This method is less strict than so-called “identity preservation”, which is obtained by physically isolating the product according to origin, thus ensuring that the grower can be directly identified. But it is more strict than the “book and claim” system, which does not trace product origin at all. The mass balance model is considered relatively resource intensive, and the European Commission aims to re-evaluate its audit procedures, meaning there is a chance that the model could be abandoned.

Given that the technical and financial requirements for auditing and compliance with certification are high, large scale corporate production often has an advantage over smallholder farmers. Throughout Southeast Asia smallholders have difficulty

accessing certification schemes and, while some advances have been made in some schemes, further steps are needed to enable smallholder farmers to gain market access.

### Awaiting proposed amendments from the European Commission

The development of the EU-RED has been highly controversial. The main policy debate so far has been on the consequences of indirect land use change (ILUC). Statistical analyses have demonstrated that ILUC-based emissions significantly reduce the environmental benefits of the EU-RED. In 2011, influenced by a stand-off between the Directorates General (DGs) in the European Commission, the DG for Energy and DG for Climate Action agreed on a seven-year delay in setting out concrete actions on ILUC. However, communications from the Commission suggest that it is continuing the work on proposals to promote “low-ILUC” biofuels via amendments to the EU-RED and the Fuels Quality Directive (2009/30/EC). It remains to be seen whether these amendments may move the EU-RED towards a more holistic view on “sustainable” biofuels and address the fact that the EU currently does not live up to the guidelines of the UN Human Rights Council in “Protect, Respect and Remedy: a Framework for Business and Human Rights”, including the need for business to ensure consent from affected communities in producer countries.



Palm nuts harvested for palm oil production

## Policy recommendations for the European Parliament, European Commission, EU member states and market actors

- **Align the EU-RED with the “policy coherence for development” agenda.** The EU aims to ensure policy coherence for development in all its sectoral policies. From this perspective, the severe impacts of palm oil cultivation on livelihoods, water resources, land management, and ecosystem services in producer countries ought to stimulate immediate action in the European Parliament and the EU member states.
- **Include stricter and mandatory criteria for water resource and land use management in the EU-RED.** The current dominant emphasis in the EU-RED on GHG emissions diverts attention from other political priorities, such as water resource management, land use planning and local livelihoods. Criteria to safeguard ecosystem benefits derived from river basin and landscape management should be included in the sustainability criteria and made mandatory in member states’ implementation, including certification schemes. These criteria should also emphasise opportunities for smallholder farmers to gain market access.
- **The forthcoming revision of the EU-RED should incorporate the principle of “free, prior and informed consent” (FPIC).** The EU member states have undersigned the UN document “Protect, Respect and Remedy: a Framework for Business and Human Rights”, and its requirement for businesses to ensure consent from affected stakeholders. Implementation of this UN framework will require that all certification schemes include the principle of FPIC.
- **Prioritize more robust sustainability standards.** Sustainability standards, such as those included in the EU-RED, differ in the extent to which they address impacts on natural resources and livelihoods in producer countries. European companies and government agencies should carefully scrutinize the rigour of such schemes when selecting and endorsing specific standards as part of national implementation programmes.
- **Strengthen traceability and transparency in the audit trail.** This will reward governments and companies that follow formal requirements and actively promote espoused sustainable water and land management strategies. The principle of “identify preservation” should be applied, so that the responsible grower can be identified. Any downgrading of requirements for traceability will work against sustainable production.
- **Strive to embed RSPO requirements in bilateral and multilateral trade agreements.** The RSPO would be strengthened if its standards were embedded in bilateral and multilateral trade agreements. Such trade agreements are legal options that are expressly permitted and encouraged in the EU-RED, but no member states have so far pursued this option.
- **Incorporate sustainability standards, such as those offered by the RSPO, into the CSR policies of European buyers.** RSPO-certified sustainable palm oil does not yet yield a direct financial premium, which is reflected in a lack of interest on the part of buyers and retailers. This poses questions about when businesses will pro-actively move to embed standards, such as the RSPO, in their CSR policies. This applies to all trade in palm oil, including that used for energy, food and cosmetics.
- **Ensure that equal attention is paid to the audit trail for palm oil used for non-energy purposes.** Future interventions must take account of the fact that general market signals and prices can have equal (or even more important) effects than tariffs and subsidies originating from the EU-RED. This is as much the case for palm oil used for non-energy purposes such as food or cosmetics (the majority of EU imports) as it is for palm oil used for fuel.

This policy brief is based on the following SEI reports:

Larsen, R. K., Osbeck, M., Jiwan, N., Rompas, A., Nito, J. and Tarigan, A. (forthcoming, 2012): *Competing Water Claims in Biofuel Feedstock Operations in Central Kalimantan: Community Grievances and Pathways to Improved Governance of Oil Palm Concessions*. SEI Working Paper.

Polpanich, O., Osbeck, M. and Naruchaikusol. (forthcoming, 2012): *Balancing Land Resources for Food vs Energy: Small-scale Land Conversion to Lucrative Oil Palm Crops*. SEI Project Report.

Sam, C. and Osbeck M. (forthcoming, 2012): *Cambodia: Current Status of Feedstocks for Biofuels*. SEI Project Report.

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