



SMALLHOLDERS AND SUSTAINABLE PALM OIL

REALISTIC IMPLEMENTATION OF RSPO PRINCIPLES AND CRITERIA

Discussion Paper

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EXECUTIVE SUMMARY

The Roundtable on Sustainable Palm Oil (RSPO) has agreed on a set of Principles and Criteria (P&C). Smallholders, who are responsible for a substantial share of palm fruit (FFB) production, need to have the knowledge and the resources to implement the P&C. Otherwise market barriers for smallholders would be the result.

Smallholders are smaller producers of FFB who own or lease land and who deliver to the market. They should be clearly distinguished from other groups in the vicinity of mills and plantations, such as settlers, contract workers, original (tribal) people and villagers.

The centre of the oil palm production system is the mill. Both large estates and smallholders deliver to the mill. Because of the need for immediate processing, there is a strong interdependency between mill and all FFB producers, including smallholders. In Malaysia and Indonesia, there are a variety of mill-smallholder situations. We distinguish three typical settings:

1. smallholders in Malaysia, who have obtained land titles as a result of government schemes (mainly FELDA). These are well-trained smallholders with strong relations with their mills;
2. smallholders in Indonesia, who work in partnerships with larger estates. Also here, the relationships between the mill and the smallholders are well developed.
3. smallholders in areas of rapid and massive growth of plantations. The relationships between smallholders and mill are not well established yet. There may be a lack of management capacity and mill capacity problems, at the disadvantage of smallholders.

For implementing RSPO P&C, the mills are the central control point. Mills should integrate RSPO P&C not only in their contracts with smallholders but also in their training and quality control programs. Evidently, this is only feasible if there are well established relationships between the mill and its smallholder suppliers, which is the case in the first two settings, but not in the third setting.

We recommend to start pilots for implementing RSPO, with a central responsibility of the mills, in settings similar to the first two settings only.

I. INTRODUCTION

I.1 Background

RSPO

The Roundtable on Sustainable Palm Oil (RSPO) has agreed on a set of principles and criteria (P&C) for sustainable palm oil. The next step will be to test their implementation. The position of smallholders is an important issue. The RSPO criteria should not create barriers for smallholders. Smallholders should have the knowledge and the resources to implement the RSPO criteria.¹

At the second RSPO General Assembly, a motion was tabled asking for (among other things) “diagnostic surveys of smallholder situations and views” and “executing activities and document trials of the application of the P&C with smallholders”. A Smallholder Task Force was set up.

Partnership between Indonesia, Malaysia and The Netherlands

In the context of the Partnership between Indonesia, Malaysia and The Netherlands on Market Access for Palm oil, implementation of the RSPO criteria is a major issue.

The Dutch Ministry of Agriculture (LNV) has commissioned the authors to write this paper as an input into a workshop in The Hague on March 1, 2006, organised by the Partnership. It is meant as an input (among other inputs) into the discussion, not as a final analysis of the situation. There may be a need for updating the information used and taking additional points of view into account.

I.2 The Questions

The following questions are important in today’s discussion:²

- How can it be guaranteed that not only large estates but also small holdings will conform to the P&C of the RSPO?
- How can potential disadvantages to smallholders in the implementation of RSPO P&C be avoided? How can be guaranteed that smallholders have the knowledge and resources required to implement the RSPO P&C?

¹ Smallholders are being mentioned explicitly in the preamble of RSPO principles and criteria and specifically in Criterion 4.8 (on training of workers, smallholders and contractors) and Criterion 6.10 (“Growers and millers deal fairly and transparently with smallholders and other local businesses”).

² The discussion in this paper is limited to the problem of implementation of RSPO P&C by smallholders. The paper does not pretend to give a full discussion of the social and economic position of smallholders in the Malaysian and Indonesia oil palm sectors.

Answers to these question can only be given on the basis of practical experience based on well-designed pilot projects. In this paper, we show that there are no simple answers to these questions. There are many nationally and regionally different smallholder situations that ask for different solutions.

1.3 Structure of this Paper

In this paper, we

- clarify what we mean by ‘smallholders’ and distinguish ‘smallholders’ from other groups of people living in the vicinity of the estate or the mill (Chapter 2);
- show that the relationships between the ‘smallholder’, the mill and the estate are regionally different, which has a consequence for the ease or the difficulty of implementing RSPO P&C. We will give three different settings as an example (Chapter 3);
- give some suggestions for implementing the RSPO P&C in the varying settings (Chapter 4);
- propose questions for the discussion on March 1, 2006 (Chapter 5).

2. SMALLHOLDERS AND OTHER RELEVANT GROUPS

2.1 Smallholders and other groups

Oil palm plantations and oil mills are surrounded by different local communities, which all have their own role and/or position towards the palm oil industry. For a good discussion, it is important to understand these roles properly. Smallholder issues should be clearly distinguished from issues related to other groups.

2.2 Smallholders

A smallholder is anyone who owns/leases land planted with oil palm trees and who produces fresh fruit bunches (FFB) for the market (and who is not a large palm oil estate)³. Holdings can be as small as 5 ha, but also more than 100 ha. A

³ This definition describes the smallholder as a main player in the palm oil supply chain: the small farmer who delivers FFB. This is not the only way to describe (oil palm) smallholders. There are alternative definitions that focus more on socio-economic aspects.

lot of 10 ha can be managed by one family⁴. As the harvested FFB has to be processed quickly, the smallholder depends on a nearby oil mill for his income.

Smallholders hold about 30 % of all Indonesian planted area and 10 % of the Malaysian planted area.

In Malaysia, an additional 30 % of the planted area has been cultivated under Government (FELDA, FELCRA and RISDA) and State Schemes. These Schemes aim at economic development of rural areas to improve the income of poor landless people. The schemes include a three stage development program, by which the participants are first trained in basic agricultural techniques, then learn how to run a small plantation block and finally get a land title for the block, by which they become a smallholder.

In Indonesia, the PTPN State Plantations, which cultivate a vast area for the production of palm fruit bunches, also have a program to encourage production by smallholders. Up till now, 10 to 50% of their area has been transferred to smallholders (so-called plasma farmers). Private plantations which mostly lease their land from the state have to run small holders programs, too. They have to transfer about 30% of their cultivated land to plasma farmers. The farmers are first trained in agricultural and management techniques before they receive a land title.

It is clearly a policy of the Indonesian and the Malaysian governments to encourage the production of FFB by smallholders to create employment for local people. The number of smallholders is likely to increase. Without appropriate solutions for smallholders, the RSPO P&C cannot be implemented.

2.3 Other Groups

Settlers

These are people coming from another region, more than often without clear land use or property rights. They may express property claims on plantation land, which may be a source of conflicts.

In Malaysia, the government and state schemes for landless settlers aim at integrating settlers into the plantation systems (see above). Such settlers are not yet smallholders, because the agencies factually manage the plantation blocks.

In Indonesia, state and the private plantations have programs for Transmigration Corporate Farming Projects as well,

Contract workers.

A plantation needs two to three workers for harvesting and field work in a block of 20 ha. In some regions, because of a shortage of local workforce, immigrants

⁴ In some schemes, small lots of 2 ha are given to settlers/smallholders. This is not enough for family income. In this case, FFB production provides small amounts of cash to supplement production of vegetables etc. for own use.

are contracted on a temporary basis. They may constitute up to 90% of the workforce. The majority of contract workers live on the estate.

Original (tribal) people

In some regions, original (tribal) people live in the vicinity of oil palm plantations. They do not have direct relationships with the oil palm industry. There may be conflicts of interests, however. These are outside the scope of this paper.

Villagers

Villagers living nearby estates and mills provide the palm oil industry with a variety of services, such as transport of FFB and CPO, maintenance of equipment and even unloading FFBs on the oil mill site. Most estates also invest into local community development (medical services, schools, delivery of good quality drinking water etc.).

3. SMALLHOLDER – MILL RELATIONS: THREE SETTINGS

3.1 A Variety of Situations: Introduction

A Typical Situation

The centre of the palm oil production system is the oil mill. All producers, large estates and smallholders, have to bring their FFB to the mill at exactly the right moment. Because of the immediate need for processing, producers do not have an alternative: the fruit bunches have to be processed by a mill in the immediate vicinity of palm fruit production.

There are many situations with respect to production capacities, the share of smallholders in total mill inputs, etc. We now sketch a typical situation (see figure).

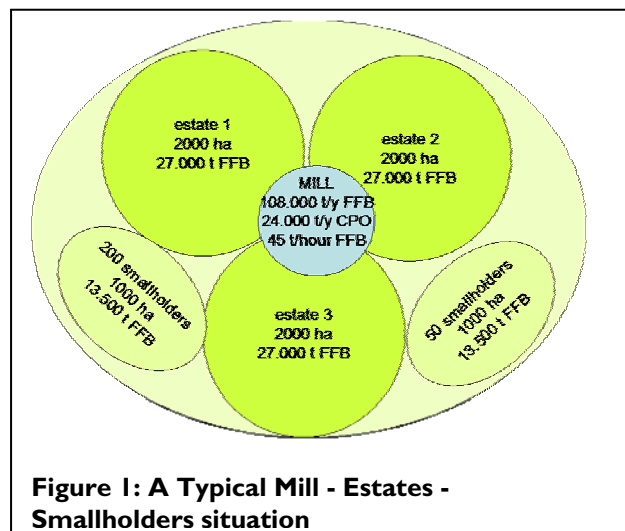


Figure 1: A Typical Mill - Estates - Smallholders situation

- The centre of the system is a palm oil mill with a production capacity of about 108.000 tons palm fruit (FFB) per year or 45 tons per hour (2400 productive hours).
- Three large estates (2000 ha each, of which 1500 mature) deliver to the mill in total 81.000 tons/year, supposing a productivity of 18 tons/year/mature ha. At each estate, there are about 280 workers.

- In this example, smallholders represent some 25% of total production input: there are 200 smallholders with an average of 5 ha and 50 smallholders with an average of 20 ha, 2000 ha in total, producing 27.000 tons/year. The share of smallholder input may be higher.
- A small holding of 5 ha (250 m x 200 m) has about 500 trees, producing 67,5 tons (or more) FFB /year. Once in 14 days, the smallholder makes a round and will deliver 2,5 tons of palm fruit to the mill = 100 to 150 fruit bunches, which he transports to the road side for further transport to the mill, normally only after a quality inspection by the mill.
- In some cases, productivity may be substantially higher, e.g. 20 tons/ha/year, requiring a higher mill capacity, e.g. 90 tons/hour. Depending on the situation, smallholder productivity may be higher or lower than productivity of the estates.
- With these dimensions, the distance between the smallholder's land and the mill will generally not exceed 20 km.
- There may be local traders (middlemen) involved. In that case, they buy the palm fruit bunches from the smallholder and deliver them to the mill.

Variations

There are many different situations that have their impact on the relationships between the mill and smallholders delivering to that mill.

- linkage to estates
Many mills have their own estates on land that they own or lease, but there are also mills that only source from estates owned by others.
- linkage to smallholder programs
The different programs in Indonesia and Malaysia for the development (such as FELDA in Malaysia, PIR-NES and PIR-TRANS in Indonesia) have different impacts on the position of smallholders, their financial situation and their relationship with the oil mills.
- mill capacity in relation to supply
As palm fruit has to be processed just in time, it is important to have sufficient mill capacity to process all fruit bunches from (a) own estates, (b) neighbouring estates and (c) smallholders. There can be a (temporary) imbalance because of rapidly expanding oil palm plantations, especially in newly developed areas. This may lead to situations in which smallholders cannot timely deliver their production to the mill.
- contract conditions between mill and smallholders
with regard to
 - quality requirements and quality systems, including the grading system;
 - guaranteed purchase of fruit bunches;
 - price-setting mechanism;

- prefinancing conditions, practices of dealing with indebted farmers.
- role of the mill in supporting smallholders with advice, training and support
As a rule, mills, in their own commercial interest, support their smallholders with a number of services, in order to enable them to deliver the right quality.
- organisation degree of smallholders
Smallholders may be organised to a different degree. There is hardly any public information about the role of smallholders organisations available.
- land ownership and leasing
Smallholders may own or lease their land. In some regions, there may be problems with land rights, especially if there are no well-established land registers. Plantations may own their land or lease it from the government or even from smallholders.
- quality of smallholder land
Smallholders may occupy land that is less favourable for oil palm growth than the estate land. It may be situated on slopes, for example. This may make it more difficult to implement RSPO criterion 4.3 (on erosion and soil degradation).
- alternative income sources for smallholders
Palm fruit may be virtually the only source of income for a region. In other regions, especially closer to cities, palm income is competing with other income. A result may be that the second generation smallholders seek urban employment rather than continuing oil palm cultivation.

Implementing RSPO Principles and Criteria

RSPO Principles and Criteria can best be integrated into the existing relationships between mill, estates and smallholders. Any other solution will be costly and probably ineffective. In many cases, there are already well-established and stable relationships between the mill and the smallholders, which form a good basis for implementing RSPO P&C. In some cases, however, these relationships have not been established (yet) and implementing RSPO P&C will be difficult, at least at the short term. Below we describe three different situations.

3.2 Setting 1: Strong Position of Smallholders by Government Regulation

The well trained smallholders originating from the government. and states schemes in Malaysia have a relatively strong position because they are mostly nearby one of the of mills spread over the country.

As a rule, these smallholders have long relationships with their mills. The smallholders sell their FFB to the mill on a contract basis. The mill uses the MPOB grading system for classifying the FFB quality. Mill inspectors are trained by MPOB as well. The FFB price is a transparent market price.

FFB production per smallholder is relatively small, say between 50 and 100 ton per year. When a mill is sourcing its FFB from smallholders only, it has to deal with 500 to 1000 producers.

3.3 Setting 2: Partnership Alliance between Mill and Smallholders

The Indonesian government's policy is to restructure a part of large estates into smaller smallholder lots. As a rule, newly established estates can only lease from the government on the condition that they simultaneously set up small holdings for local people.

The smallholders work in a partnership alliance with the larger estates, which mostly have their own mill that also provides the smallholders with advice and services.

The smallholders sell their FFB on the basis of contracts with mills, which include a grading system and mostly a transparent pricing system. The services provided to the smallholders are in the economic interest of the mill, to ensure that smallholders deliver the right FFB quality.

In this setting, the estate actively invests into community development, too, by giving employment to local people, investment in medical clinics, schools etc.

3.4 Setting 3: Smallholder-Mill Relations in a Complex and Turbulent Situation

In some regions, there is a rapid and massive expansion the oil palm business. Large numbers of settlers and smallholders are starting new plantations, not always with sufficient expertise and guidance.

Typical phenomena in this setting are:

- Smallholders start without appropriate farming experience;
- There is a shortage of experienced mill management;
- At times, there may be insufficient mill capacity, which may incur losses for smallholders;
- The relationship between smallholders and mill is not well established yet.

In these areas, many new mills without own estates are being setup. These mills cannot do much more than check FFB quality at the mill gate. They may refuse FFB deliveries, not only when there is a quality problem, but also in case of an oversupply situation.

In this setting, conditions for implementing RSPO Principles and Criteria for smallholders are not favourable. For effective and efficient implementation of RSPO P&C, there is a need for well-established and stable relationships between smallholders and the mill.

4. SMALLHOLDERS AND THE IMPLEMENTATION OF RSPO CRITERIA

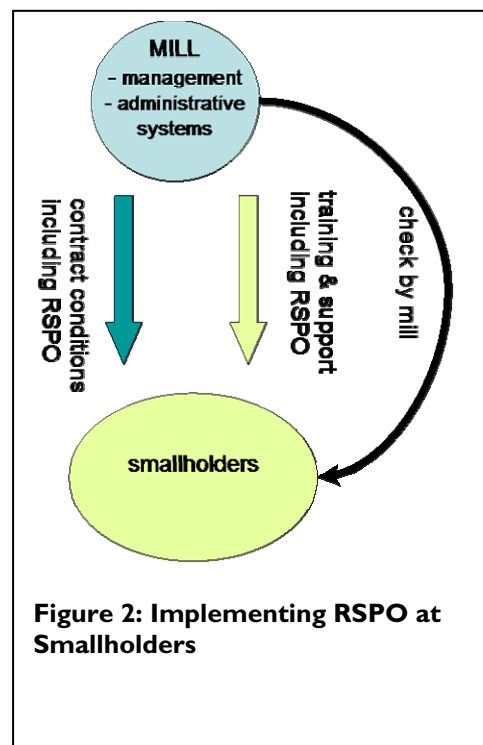
4.1 RSPO, Smallholders and the Mill

For implementing the RSPO Principles and Criteria (P&C), the palm oil mill is the critical control point. Only the mill has the possibility and can therefore bear the responsibility to make sure that the RSPO Principles and Criteria are being implemented:

- at the estates owned by the oil mill company;
- at other estates delivering to the mill;
- at smallholders delivering to the mill.

A practical way of verifying oil palm plantations is probably to verify the mill rather than the plantations. The picture could look like this:⁵

- The mill can acquire the RSPO certificate if it can give the required certainty that (all or a sufficient percentage of) FFB deliveries conform to RSPO criteria.
- RSPO P&C could become part of the standard contract between the mill and all parties who deliver palm fruit bunches, including smallholders.



- The mill regularly checks whether the smallholders conform to RSPO criteria. These checks can most probably best be added to existing checks for quality control reasons.
- The mill provides the necessary training and assistance to enable smallholders to implement the RSPO criteria. We expect that this training can become part of an overall training package including quality and grading issues.

⁵ The issue of verification/certification is still to be discussed and decided by the RSPO. The following text only gives a first idea of how the situation could look like from a technical point of view if there is a clear wish to verify small oil palm holdings.

4.2 Recommendation for Pilots

Setting 1 and 2

In Setting 1 and Setting 2, there are well-established relationships between the smallholder and the mill. The existing quality control system can be used as a starting point for implementing RSPO P&C and for training smallholders, as discussed above.

Pilots should be used to find workable models for this integration into the existing systems. We recommend to start pilots at well-organised mills with good quality systems in areas with a longer existing structure of estates and smallholders. As a result of the first pilots, a model (or regionally adapted models) for implementation RSPO for smallholders can be defined. This model can then be used for training purposes and implementation at other, potentially more difficult, mills.

For mills, in which the quality systems have not yet been fully developed and in which there is a need for improving mill-smallholder relations, pilot projects that combine the development of quality and implementation of RSPO could be an option.

Setting 3

In Setting 3, which is characterised by a high level of uncertainty and mill-smallholder relations that are not stable yet, implementation of RSPO P&C appears to be premature and difficult. It is premature since there are other priorities in such a situation: constructing the appropriate mill capacity, training the management and organising quality assurance. Only after these steps, minimal conditions for successful implementation of RSPO P&C will be present

5. QUESTIONS FOR THE DISCUSSION ON MARCH 1, 2006

Question 1:

What are the pros and cons of having the oil mills to play a centrally responsible role in implementing RSPO P&C at smallholders? What are the alternatives? Are the mills willing to take on this responsibility?

Question 2:

How are smallholders organised? What are the relevant organisations? What (supplementary) role can be played by smallholder organisations in supporting the smallholders in implementing RSPO P&C?

Question 3:

Is it a good idea to start smallholder pilots for RSPO P&C within the framework of well organised government and/or business driven outgrower schemes (FELDA, mill-smallholder partnerships in Indonesia)?

Question 4:

Are there feasible options for verifying oil palm plantations of individual smallholders, who are not participating in any well-structured outgrower scheme, with respect to RSPO P&C?

Question 5:

What can be the Partnership's role in promoting a feasible path to realistic implementation of RSPO P&C at the smallholder level in Indonesia and Malaysia? How should the Partnership cooperate with the RSPO Smallholder Task Force?