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Executive summary

This paper analyses the provisions for sustainable palm oil included in the Comprehensive Economic Partnership Agreement (CEPA) between Indonesia and the European Free Trade Association (EFTA) states (Iceland, Lichtenstein, Norway and Switzerland). It considers whether similar provisions could be included in the Free Trade Agreement (FTA) currently being negotiated between Indonesia and the EU and suggests ways forward for future trade agreements aimed at promoting trade in sustainably produced palm oil.

The Indonesia–EFTA CEPA entered into force on 1 November 2021. Article 8.10, on ‘Sustainable Management of the Vegetable Oils Sector and Associated Trade’, contains commitments to: ‘apply laws, policies and practices aiming at protecting primary forests, peatlands, and related ecosystems, halting deforestation, peat drainage and fire clearing in land preparation, reducing air and water pollution, and respecting rights of local and indigenous communities and workers’ in the production and trade of vegetable oils.’

The trade concessions for vegetable oils – which, in the Indonesian context, essentially means palm oil – are decided by each Party to the agreement. Of the EFTA STATES, to date only Switzerland has set out in detail how it intends to implement them, by establishing a series of reductions in import duties (within agreed quotas) for palm oil, palm stearin and palm kernel oil where it meets the criteria. Compliance with the criteria is demonstrated through importing palm oil certified to the standards of the Roundtable on Sustainable Palm Oil (RSPO) (Identity Preserved or Segregated); the International Sustainability and Carbon Certification (ISCC) Plus Segregated; or the Palm Oil Innovation Group (POIG) (combined with RSPO Identity Preserved or Segregated) systems.

In practice, the impact of these provisions is likely to be insignificant. Switzerland imports very little palm oil from Indonesia, most of it is already certified to RSPO Segregated Standards, and most of it already benefits from low or zero import duties. Nevertheless, the system established by Switzerland may provide a precedent for future trade agreements.

This is of particular relevance to the ongoing negotiations for an FTA between Indonesia and the EU, a far more important market for exports of Indonesian palm oil. Indonesia has proposed the inclusion of language on sustainable vegetable oils, but under its proposals, ‘sustainability’ is to be verified through standards established by either party – which would mean that the Indonesian Sustainable Palm Oil (ISPO) scheme would have to be recognised by the EU. The EU has yet to make a counter-proposal.

It is certainly possible that the EU could accept the general principle of discriminating in trade on the basis of the way in which products are produced, as in the EFTA CEPA. Certification schemes could also be used to demonstrate compliance with the criteria, as they are used to decide eligibility for support for the use of vegetable oils for biofuels under the EU Renewable Energy Directive. It is highly unlikely, however, that any criteria acceptable to the EU would include ISPO-certified palm oil, given the numerous shortcomings of the ISPO scheme.
The following steps would help maximise the outcomes of a future Indonesia–EU FTA in terms of support for trade in sustainably produced palm oil:

- Careful and detailed definitions of criteria for sustainable palm oil, covering all relevant environmental, social, labour and human rights issues.

- Review of the criteria by a multi-stakeholder process, including representatives of oil palm farmers, particularly smallholders, local communities and civil society organisations, alongside government and industry.

- The offer of support from the EU to improve the criteria, implementation and monitoring of the ISPO scheme to enable it to meet ambitious sustainability criteria.

- The inclusion in the FTA of elements drawn from the Voluntary Partnership Agreements (VPAs) of the EU’s Forest Law Enforcement, Governance and Trade (FLEGT) Action Plan. These could include Indonesian commitments to improve governance and law enforcement; to improve transparency and multi-stakeholder input to decision-making; and to establish a robust and independently verifiable traceability scheme, in exchange for improved access to the EU market and capacity-building assistance from the EU, including support for smallholder farmers.
1 The EFTA–Indonesia CEPA and palm oil

Negotiations on a broad-based Free Trade Agreement (FTA) between Indonesia and the European Free Trade Association (EFTA) states (Iceland, Lichtenstein, Norway and Switzerland) were launched in July 2010 and concluded in December 2018, with the signing of the Comprehensive Economic Partnership Agreement (CEPA). After ratification by all parties to the agreement, the CEPA entered into force on 1 November 2021.

The agreement covers trade in goods and services, investment, intellectual property rights, government procurement, competition, trade and sustainable development, and cooperation. In the area of trade in goods, the EFTA states are to abolish all customs duties on imports of industrial products, including fish and other marine products, originating in Indonesia. Indonesia will gradually eliminate or reduce customs duties on industrial products, including fish and other marine products, originating in an EFTA state.

The agreement contains several references to sustainable development, including in the clauses setting out the objectives of the agreement. Chapter 8 is devoted to ‘Trade and Sustainable Development’. It contains the commitment to ‘promote the development of international trade in such a way as to contribute to the objective of sustainable development’ (Article 8.1(2)) and recognises that ‘economic development, social development and environmental protection are interdependent and mutually reinforcing components of sustainable development’ (Article 8.1(3)).

Most of Chapter 8 is similar in outline to trade and sustainable development chapters in recent EU trade and investment agreements: a recognition of the importance of the issue. It can also be seen as a commitment to uphold standards of environmental and labour protection, including not lowering standards to attract investment or to realise a competitive trade advantage. The chapter references various international agreements, including multilateral environmental agreements, particularly the Convention on International Trade in Endangered Species (CITES) (included in the article dealing with sustainable forest management) and International Labour Organisation (ILO) conventions.

There is also a commitment to ‘promote the development and use of certification schemes for forest-related products from sustainably managed forests’, and a specific reference to the use of legality assurance systems for timber, as required by the EU–Indonesia Voluntary Partnership Agreement (VPA) established under the EU’s Forest Law Enforcement, Governance and Trade (FLEGT) Action Plan (Article 8.8(2) (b) and (c), respectively).

None of these commitments directly affect trade between Indonesia and the EFTA states. The exception is Article 8.10, on ‘Sustainable Management of the Vegetable Oils Sector and Associated Trade’ (see Box: Article 8.10).

1 Available at https://www.efta.int/sites/default/files/documents/legal-texts/free-trade-relations/indonesia/efta-indonesia-main-agreement.pdf.
ARTICLE 8.10
Sustainable Management of the Vegetable Oils Sector and Associated Trade

1. The Parties recognise the need to take into account the economic, environmental and social opportunities and challenges associated with the production of vegetable oils and that trade between them can play an important role in promoting sustainable management and operation of the vegetable oils sector.

2. With a view to ensuring economically, environmentally and socially beneficial and sound management and operation of the vegetable oils sector, the Parties commit to, inter alia:

(a) effectively apply laws, policies and practices aiming at protecting primary forests, peatlands, and related ecosystems, halting deforestation, peat drainage and fire clearing in land preparation, reducing air and water pollution, and respecting rights of local and indigenous communities and workers;

(b) support the dissemination and use of sustainability standards, practices and guidelines for sustainably produced vegetable oils;

(c) cooperate on improving and strengthening government standards where applicable;

(d) ensure transparency of domestic policies and measures pertaining to the vegetable oils sector; and

(e) ensure that vegetable oils and their derivatives traded between the Parties are produced in accordance with the sustainability objectives referred to in subparagraph (a).

The trade concessions for vegetable oils – which, in the Indonesian context, essentially means palm oil – are decided by each Party to the agreement, along with concessions on other agricultural products. Of the EFTA states, to date only Switzerland has set out how it intends to implement the provisions relating to palm oil (see below); as by far the largest economy in the EFTA area, it is in any case the most significant. Iceland and Norway have both published tariff schedules including zero import duties for all or most types of palm oil, as long as they are compliant with the provisions of Article 8.10, but no information appears to be available on the implementation of this requirement.  

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2 - See Indonesia–EFTA CEPA Annex III, Schedule on Tariff Commitments on Goods: Commitments of Iceland on Goods Originating in Indonesia; and Annex IV, Schedule on Tariff Commitments on Goods: Commitments of Norway on Goods Originating in Indonesia. Lichtenstein is part of a customs union with Switzerland, so does not maintain separate tariff schedules.
1.1 Implementation of the palm oil provisions: Switzerland

The Swiss tariff preferences for imports of Indonesian palm oil include a series of tariff-rate quotas for different products (quota A for raw palm oil, quota B for palm stearin, quota C for palm kernel oil) which apply reductions in import duties of between 20 and 40 per cent for imports up to the quota volume ceiling; annual growth in the ceilings is allowed for a period of five years. Quotas B and C, for palm stearin and palm kernel oil, have two levels, with higher import duty reductions for the initial volume.

• Quota A: 1,000 tonnes for raw palm oil, 30 per cent tariff reduction, annual growth of 50 tonnes over five years to 1,250 tonnes.

• Quota B1: 5,000 tonnes for palm stearin, 40 per cent tariff reduction, annual growth of 250 tonnes over five years to 6,250 tonnes.

• Quota B2: 1,000 tonnes for palm stearin, 20 per cent tariff reduction, annual growth of 50 tonnes over five years to 1,250 tonnes.

• Quota C1: 2,000 tonnes for palm kernel oil, 40 per cent tariff reduction, annual growth of 100 tonnes over five years to 2,500 tonnes.

• Quota C2: 1,000 tonnes for palm kernel oil, 20 per cent tariff reduction, annual growth of 50 tonnes over five years to 1,250 tonnes.

The trade preferences are only to be granted if the palm oil imported has been produced entirely in Indonesia and in accordance with the conditions set out in Article 8.10 of the CEPA.

The key issue, of course, is how this compliance can be demonstrated. A draft regulation was published in December 2020 and was open to consultation until April 2021. Responses to the consultation were overwhelmingly supportive; no respondent objected to the proposed system, though various proposals for changes in detail were suggested. A number of respondents observed that the regulation represented a good model for future trade agreements. A slightly revised regulation was adopted in August and entered into force once the agreement itself did, i.e. on 1 November 2021.

The regulation sets out the government’s system to require importers wishing to import palm oil from Indonesia at the preferential rate to provide proof of compliance with the sustainability goals set out in Article 8.10 of the CEPA. Importers are to do this by providing evidence of certification of the products against standards which incorporate the sustainability provisions of Article 8.10.

Rather than establish its own control system, the government decided to assess whether existing certification schemes for palm oil were adequate to meet these criteria; as the explanatory note accompanying the regulation explained, ‘Switzerland has neither the possibility, the expertise nor the resources to carry out on-site inspections in Indonesia.’ The State Secretariat for Economic Affairs (SECO) commissioned an evaluation of five established schemes; this was overseen by the Federal Office of the Environment, WWF and the Swiss Palm Oil Network (which includes importers, supermarkets and companies), and conducted by a consultancy, Christof Walter Associates. The schemes assessed were those of the:

3- See Indonesia–EFTA CEPA Annex V, Schedule on Tariff Commitments on Goods: Commitments of Switzerland on Goods Originating in Indonesia; and Swiss Federal Department of Economic Affairs, Education and Research, Fact sheet: Comprehensive Economic Partnership Agreement (CEPA) between the EFTA States and Indonesia (February 2021).

4- The notice of the consultation is available at https://fedlex.data.admin.ch/eli/dl/proj/6020/73/cons_1; the draft regulation is available at https://www.newsd.admin.ch/newsd/message/attachments/64592.pdf.

5- The final regulation, explanatory note and results of the consultation are available at https://www.admin.ch/gov/de/start/dokumentation/medienmitteilungen.msg-id-84740.html.

6- Regulation on the Import of Sustainably Produced Palm Oil from Indonesia at the Preferential Rate of Duty: Explanations on the Ordinance (State Secretariat for Economic Affairs, August 2021), Section 2 (unofficial translation).

• Roundtable on Sustainable Palm Oil (RSPO). The RSPO scheme offers four supply chain models; only the identity preserved model (where the palm oil from a single identifiable certified source is kept separately from conventional palm oil throughout the supply chain) and the segregated model (where sustainable palm oil from different certified sources is kept separate from conventional palm oil) were evaluated. The mass balance and book-and-claim models were not considered adequate to prove compliance with the criteria, as they provide administrative but not physical traceability.

• International Sustainability and Carbon Certification (ISCC). The ISCC scheme is extensively used for vegetable oils for biofuels; ISCC Plus is the standard for other uses, including foodstuffs. Similarly to RSPO, ISCC offers segregated and mass balance chain-of-custody models; only the segregated model was evaluated.

• Palm Oil Innovation Group (POIG). A multi-stakeholder initiative, POIG aims to promote the adoption of responsible palm oil production practices going beyond the RSPO standard. The POIG Charter requires certification to RSPO standards together with adherence to the Charter, which covers criteria relating to environmental responsibility, partnerships with communities and workers’ rights and corporate and product integrity.

• Rainforest Alliance Sustainable Agriculture Standard. An international NGO, Rainforest Alliance focuses on sustainability certification of forestry, agriculture and tourism. Its palm oil standard is due for revision in 2022, and it will incorporate a requirement for RSPO certification as well as its own criteria.

• Bio Suisse Organic. Bio Suisse is the umbrella organisation of Swiss organic producers and producer associations, certifying products to organic standards. Like Rainforest Alliance, Bio Suisse is planning to change its rules to require RSPO certification as a prerequisite for its own certification.

In practice, most certified palm oil worldwide is covered by the RSPO or ISCC schemes (though not necessarily by the segregated or identity preserved models). Many organisations certified to Rainforest Alliance standards and some to Bio Suisse organic standards tend to be certified by RSPO as well.

The Indonesian national palm oil sustainability standard, ISPO, was not included in the assessment; as the study commented:

“The Indonesian Sustainable Palm Oil Standard (ISPO) has currently no relevance in the Swiss market and is unlikely to gain a more prevalent position in its current form, as several studies have found it to compare poorly to other standards … The benchmark for ISPO was hence not included in this report, though we reference findings regarding ISPO from other studies and a short description. It is worth noting that ISPO is currently under review. The forthcoming version of ISPO may prove to be more relevant for the Swiss industry and could be included in a future evaluation.” 10

8 - Under the mass balance model, certified palm oil is mixed in with conventional palm oil but monitored administratively; users can advertise their product as partially certified, usually with a specific percentage figure. Under the book-and-claim model, certified palm oil is not kept apart, but suppliers of certified palm oil sell certificates to users; while the user may not actually be using any certified palm oil, they do contribute to the costs of production.

9 - Comprehensive global statistics are not available, but in recent years the use of book-and-claim certificates has fallen both in absolute and relative terms. In some European countries, segregated (including identity preserved) now accounts for the majority of imports, while in others mass balance is still significant; see Choosing Sustainable Palm Oil: Progress report on the import and use of sustainable palm oil in Europe (ESPO, 2019).

10 - Benchmarking Study on Sustainability Standards for the Palm Oil Sector, p. 3.
Improving forest governance in relation to palm oil (January 2022)

In fact by the time the study was published (May 2020), the ISPO scheme had already been reviewed and a new regulation had entered into force. See further in Section 3.) Following the completion of the agreement, the Indonesian ambassador to Switzerland commented that both countries were cooperating to strengthen ISPO certification, so that it could be entered as one of the standards in the regulation.11 This was confirmed by the Indonesian trade minister in April.12

The five standards subject to evaluation were benchmarked against an extended version of WWF’s Certification Assessment Tool. This is a formalised methodology developed by WWF to evaluate and compare standards and certification schemes; it assesses the criteria covered by the standard, including environmental, social and rights issues, together with the scheme’s governance, rules and procedures. For the purposes of the evaluation for SECO, a further 30 criteria were added to the 160 in the Certification Assessment Tool, covering additional human and labour rights requirements, criteria for monitoring and evaluating certification impacts and other good practices for palm oil mills, waste management, energy use and smallholder relations.

The study found that POIG and RSPO ranked highest, with 93 per cent and 91 per cent coverage of the benchmarking criteria, respectively. They were followed by ISCC Plus (83 per cent), Rainforest Alliance (78 per cent) and Bio Suisse Organic (58 per cent). As the report concluded, this ranking was broadly consistent with the findings of other published benchmarking studies, despite differences in methodologies and thematic focuses.

SECO accepted these findings, and chose what was felt to be the four best options: RSPO Identity Preserved, RSPO Segregated, ISCC Plus Segregated and POIG combined with RSPO Identity Preserved or Segregated. These are listed in Article 3 of the regulation. Article 7 specifies that the list of recognised standards must be regularly reviewed, with the involvement of relevant stakeholders from business and civil society, to ensure that they continue to verify compliance with the criteria. Standards can be removed from the approved list and new standards added.

An importer who has been certified according to one of these sustainability standards will be able to submit an application to SECO, which, if accepted, will authorise them to import Indonesian palm oil on the preferential basis.13 Hence, the final responsibility for acceptance lies with SECO. The importer will use the customs declaration to declare that the goods in each individual consignment meet the sustainability standard; proof of origin must also be provided, and imports must be delivered in 22-tonne tanks to facilitate traceability. The authorities will check whether the importer has the required authorisation when clearing the goods through customs, and random checks, or checks on the basis of suspicion, will also be used to confirm whether the goods in an individual consignment are certified as claimed. In the event of a violation, customs officials can levy the difference in customs duties and, potentially, apply additional penalties.

The impacts on the Swiss economy of the palm oil provisions are not expected to be significant. The government’s briefing note on the agreement stated that it assumed that: ‘Total Swiss import of palm oil will not increase as a result of the CEPA. Swiss palm oil imports from Indonesia are currently very low… It is possible that Indonesia will gain market share in the long term thanks to the agreement… Almost all palm oil intended for the Swiss food industry is already certified according to sustainability standards.’14

According to the briefing note, from 2012 to 2019, Switzerland imported an annual average of 32,027 tonnes of palm oil from around the world. Over this period, an average of 811 tonnes per year, or around 2.5 per cent of the total, came from Indonesia; this volume fell to 35 tonnes (0.1 per cent of total palm oil imports) in 2019. See Figure 1.

13 - Swiss Federal Department of Economic Affairs, Education and Research, Fact sheet on palm oil in relation to the wide-ranging Economic Partnership Agreement with Indonesia (not dated); https://www.swissinfo.ch/resource/blob/46383566/026d9252e280b03eb284d600cc51b64/info-sheet-data.pdf.
14 - Swiss Federal Department of Economic Affairs, Education and Research, Fact sheet: Comprehensive Economic Partnership Agreement (CEPA) between the EFTA States and Indonesia (February 2021).
This is a tiny proportion of total Indonesian exports of palm oil, to all destinations, of about 37 million tonnes a year. Even if Swiss importers reached the quota ceiling of 12,500 tonnes a year, this would still account for only 0.03 per cent of Indonesia’s palm oil exports (at 2019 levels). In 2020, total imports of palm oil to Switzerland fell even further, to 19,789 tonnes, though the volume imported from Indonesia – 125 tonnes – rose a little.\(^{15}\)

The Swiss Palm Oil Network, which represents the major Swiss palm oil importers and users, was established in 2020 with the aim of achieving 100 per cent certified and segregated palm oil by 2025. The latest information on their website states that this goal has already been achieved for palm oil and palm kernel oil, but not for palm stearin.\(^{16}\)

On top of this, Swiss import duties for palm oil are in any event quite low; for crude palm oil and crude palm kernel oil, for example, they are zero, as they are for several other product categories. Indonesia is included, along with most developing countries, in the Swiss Generalised System of Preferences (GSP), which sets out tariff reductions applicable to developing countries, so the country already benefits from low rates of import duty.

It is assumed, then, that if imports of palm oil from Indonesia increase up to the tariff rate quota ceilings (a total of 10,000 tonnes for all products, rising to 12,500 tonnes over five years), this will simply displace imports from other sources, for example Côte d’Ivoire, Malaysia and the Solomon Islands, the main sources of Swiss imports in 2019 and 2020.\(^{17}\)

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\(^{15}\) UN Comtrade.

\(^{16}\) See [https://palmoelnetzwerk.ch/en/the-network/](https://palmoelnetzwerk.ch/en/the-network/).

\(^{17}\) Monique Ryser, ‘Dispute over palm oil: Agreement with Indonesia breaks new ground’ (bilaterals.org, 13 January 2021); [https://www.bilaterals.org/?dispute-over-palm-oil-agreement](https://www.bilaterals.org/?dispute-over-palm-oil-agreement). For import proportions, UN Comtrade.
The provisions for palm oil played a major part in the referendum on the CEPA held in March 2021 promoted by the ‘Stop Palm Oil’ referendum committee, a coalition of civil society and agricultural groups. According to their campaign website, ‘The sustainability criteria in the agreement will have no effect. There are no effective verification mechanisms and virtually no sanctions for violations’ of the criteria in the agreement’. On 7 March 2021 Swiss citizens voted by 51.6 per cent to 48.4 per cent to endorse the CEPA, a much narrower result than had been expected; the strongest opposition came mostly from the French-speaking cantons. According to some observers, the inclusion of the sustainability criteria was critical, and the referendum would probably have been lost without them.

It seems unlikely, however, that the referendum result has brought an end to the debate. A statement by the Stop Palm Oil committee on 1 April criticised the proposed selection of certification systems, describing them as ‘labels of little relevance, which certainly sound good on paper, but show obvious shortcomings both in terms of implementation and controls’. The coalition called for a second benchmarking study to include an analysis of the application and effectiveness of the standards instead of simply their criteria; for the initial list of standards to be restricted only to POIG and RSPO Identity Preserved; and for more clarity over sanctions for non-compliance.

18 - https://stop-huile-de-palme.ch.
19 - ‘Swiss free trade deal with Indonesia narrowly survives referendum’, swissinfo.ch, 7 March 2021.
1.2 Indonesian views on the CEPA palm oil provisions

The reaction in Indonesia to the signing of the CEPA and the Swiss referendum result appears to have been broadly positive, and the Indonesian parliament approved the agreement on 9 April 2021.

There was some comment, however, on the exclusion of the ISPO standard from the Swiss list of acceptable certification systems, and as mentioned in Section 2, shortly after the referendum result, the Indonesian ambassador to Switzerland commented that both countries were cooperating to strengthen ISPO certification, so that it could be entered as one of the standards in the regulation.

Elsewhere there was some criticism of the failures of the Indonesian government and palm oil exporters to do more to combat ‘palm oil’s poor image as the major cause of deforestation’. As the world’s largest producer of palm oil, Indonesia should convince people that the crop is not the Achilles’ heel of Indonesian trade that can be targeted for tariffs and other requirements… But it will not happen if the government and the private sector continue to treat environmental problems only as a necessity to secure trade deals, instead of investing in more consistent, massive sustainability efforts that make people see that they do not harm the rainforests when they consume palm oil.

It seems unlikely that the CEPA will affect Indonesian exporters to any significant extent. As noted above, the Swiss market for palm oil is tiny, and import duties on palm oil from Indonesia are already low. If the list of acceptable certification systems is extended to include ISPO – though at present this seems highly unlikely, given concerns over the Indonesian standard – this could change, but at the moment the palm oil provisions in the CEPA seem to be mainly symbolic.

Indeed, it is the precedent that the CEPA sets for the treatment of palm oil that may be of most value to the Indonesian government in their negotiations with the EU, a far bigger importer of Indonesian palm oil. As the Indonesian Deputy Trade Minister commented in July 2021, ‘This is a positive precedent and conveys a firm, clear, and strong message to the EU public that our palm oil is acceptable and should not be discriminated against by EU countries.’

Improving forest governance in relation to palm oil

(January 2022)

Photo: Hari Priyadi/CIFOR
2 The EU–Indonesia FTA and palm oil

In 2009, Indonesia and the EU agreed a Framework Agreement on Comprehensive Partnership and Co-operation. It entered into force in May 2014. The Agreement provides the legal framework to engage and cooperate across a wide spectrum of policy fields, including human rights, political dialogue, and trade.

Following exploratory discussions on trade and investment, negotiations for an EU–Indonesia FTA were launched on 18 July 2016. The ambition is to conclude an FTA that facilitates trade and investment and covers a broad range of issues, including tariffs, non-tariff barriers to trade, trade in services and investment, trade aspects of public procurement, competition rules, intellectual property rights and sustainable development. Eleven full rounds of talks have been held so far, the latest in November 2021. A sustainability impact assessment of the FTA was launched in 2018 and the final report, prepared by the consultancy Development Solutions, was published in August 2019.

Prospects for the FTA are uncertain. The EU’s decision to identify palm oil as a feedstock at high risk of causing indirect land use change (ILUC) and therefore to phase out its eligibility for financial or regulatory support for use for energy by 2030, under the provisions of the Renewable Energy Directive, has, unsurprisingly, angered the Indonesian government, which in 2020 filed a request for a dispute case at the World Trade Organisation (WTO). They maintain that having palm oil as the only biofuel feedstock categorised as high-ILUC-risk suggests that the EU was acting in a discriminatory manner.

2.1 Indonesian palm oil and the EU

The EU is a significant importer of palm oil from Indonesia, importing between 14 and 17 per cent of Indonesian palm oil exports (by weight) in each year between 2016 and 2020; this made it the world’s third largest importer, behind India (20–30 per cent) and China (14–22 per cent). After the EU lifted anti-dumping duties on Indonesian palm oil biodiesel (and Argentine soy biodiesel) in 2018, the EU also imported substantial quantities of palm oil biodiesel – 1.2 million tonnes in 2018, compared to over four million tonnes of crude palm oil (from all sources) used to make biodiesel in European biorefineries. However, in August 2019, anti-dumping duties were reimposed provisionally on the grounds that Indonesian producers were benefiting from a range of subsidies; the measure was confirmed in December 2019.

Use for energy, mostly for biodiesel for transport, but also some for power and heat generation, is now the main destination for palm oil imports to the EU; in 2018, 65 per cent of palm oil imports were used for energy. To qualify for financial and regulatory incentives, palm oil used in energy must meet the sustainability requirements of the EU Renewable Energy Directive, which specify minimum greenhouse gas savings levels compared to fossil fuels, and also require the feedstock not to have been obtained from an area that was classified in 2008 as highly biodiverse land, land with high carbon stock, or peatland. The criteria did not include the impacts of ILUC, but as concern over these impacts grew, the EU adopted additional rules to try to limit them. The result, as noted above, was that the eligibility of palm oil to receive support for use for energy will now be phased out by 2030. Member states are allowed to phase out particular feedstocks faster if they wish. To date, Belgium, Denmark, France, Germany and Italy have all announced earlier phase-out dates for support for palm oil.

25 - UN Comtrade data for HS 1511 (palm oil and its fractions).
26 - Almost two-thirds of palm oil consumed in the EU is burned as energy – new data’ (Transport & Environment, 26 June 2019); https://www.transportenvironment.org/press/almost-two-thirds-palm-oil-consumed-eu-burned-energy-new-data.
27 - Ibid.
The Directive specifies that certification schemes may be used to demonstrate compliance with the sustainability criteria, though users may instead provide their own evidence for uncertified feedstock. A number of certification schemes have been approved by the European Commission as indicating compliance with the criteria under the terms of the 2009 Renewable Energy Directive, and the approval process for the 2018 (recast) Directive is ongoing; a preliminary positive assessment has been made of several, including the ISCC EU scheme.\textsuperscript{30} Exact data on the coverage of certification schemes for palm oil used for energy in the EU does not appear to be available, but studies suggest that the ISCC scheme is dominant.

For palm oil used for foodstuffs, the main certification scheme is the RSPO. Industry associations, and sometimes governments, in a number of EU Member States have declared commitments to achieving 100 per cent certified sustainable palm oil in their markets; by 2019, 86 per cent of palm oil used for food in the EU was RSPO-certified.\textsuperscript{31}

\textit{Import duty rates}

Indonesia qualifies for lower import duties under the EU’s standard GSP for low and lower-middle income countries. As can be seen from Table 2, this means that crude palm oil and palm kernel oil benefit from zero import duties and processed products from progressively higher rates. This is a typical example of ‘tariff escalation’, where there are higher import duties on semi-processed products than on raw materials, and higher still on finished products. These are designed to protect processing industries in the country of import and discourage the development of processing activity in the countries where the raw materials originate.

As would be expected given these different import duty rates, crude palm oil accounted for about two-thirds of Indonesia’s palm oil exports to the EU in 2019 and 2020.\textsuperscript{32}

\textsuperscript{32} UN Comtrade database, results for HS 151110 and HS 151190.
<table>
<thead>
<tr>
<th>Product code</th>
<th>Product description</th>
<th>Import duty</th>
</tr>
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<tbody>
<tr>
<td>1511</td>
<td>Palm oil and its fractions, whether or not refined, but not chemically modified</td>
<td>0%</td>
</tr>
<tr>
<td>15111010</td>
<td>Crude oil – for technical or industrial uses other than the manufacture of foodstuffs for human consumption</td>
<td>0%</td>
</tr>
<tr>
<td>15111090</td>
<td>Crude oil – other</td>
<td>0%</td>
</tr>
<tr>
<td>15119011</td>
<td>Other: solid fractions – in immediate packings of a net content not exceeding 1 kilogramme (kg)</td>
<td>4.4%</td>
</tr>
<tr>
<td>15119099</td>
<td>Other – for technical or industrial uses other than the manufacture of foodstuffs for human consumption</td>
<td>3.1%</td>
</tr>
<tr>
<td>1511901920</td>
<td>Solid fractions – other for the manufacture of fatty acids etc.</td>
<td>3.8%</td>
</tr>
<tr>
<td>1511909120</td>
<td>Solid fractions for the manufacture of fatty acids etc.</td>
<td>1.6%</td>
</tr>
<tr>
<td>1513</td>
<td>[Including] palm kernel and fractions thereof</td>
<td></td>
</tr>
<tr>
<td>1513211020</td>
<td>Crude oil, for technical or industrial uses other than the manufacture of foodstuffs for human consumption, for the manufacture of fatty acids etc.</td>
<td>0%</td>
</tr>
<tr>
<td>1513211090</td>
<td>Crude oil, for technical or industrial uses other than the manufacture of foodstuffs for human consumption – other</td>
<td>0%</td>
</tr>
<tr>
<td>1513213000</td>
<td>Crude oil, other, in immediate packings of a net content not exceeding 1 kg</td>
<td>4.4%</td>
</tr>
<tr>
<td>1513219000</td>
<td>Crude oil, other</td>
<td>2.2%</td>
</tr>
<tr>
<td>1513291100</td>
<td>Other solid fractions, in immediate packings of a net content not exceeding 1 kg</td>
<td></td>
</tr>
<tr>
<td>1513291900</td>
<td>Other solid fractions</td>
<td>7.4%</td>
</tr>
<tr>
<td>1513293020</td>
<td>Other for the manufacture of fatty acids etc.</td>
<td>1.6%</td>
</tr>
<tr>
<td>1513293090</td>
<td>Other – for technical or industrial uses other than the manufacture of foodstuffs for human consumption</td>
<td>1.6%</td>
</tr>
<tr>
<td>1513295000</td>
<td>Other – in immediate packings of a net content not exceeding 1 kg</td>
<td>8.9%</td>
</tr>
<tr>
<td>1513299000</td>
<td>Other</td>
<td>6.1%</td>
</tr>
</tbody>
</table>

Source: European Commission, Access2Markets online database.
2.2 The possible impact of the FTA

The Sustainability Impact Assessment (SIA) conducted for the European Commission assessed what the effect would be of liberalising the trade in Indonesian palm oil exports to the EU. Given the importance of the commodity to Indonesia’s economy, the topic was treated in some detail.33

In fact the modelling conducted for the SIA projected very little change in palm oil exports to the EU as a result of import duty changes:

“To this end, the Study’s Computable General Equilibrium (CGE) model projects that Indonesia will experience a marginal decrease in total sectoral output as a result of the FTA, with declines of 0.06 per cent under the conservative scenario, and a 0.04 per cent decrease under the ambitious modelling scenario. As noted in the macroeconomic assessment (see Chapter 3.2.1), this outcome is anticipated to arise through the agreement’s promotion of a reallocation of resources towards the manufacturing and export of textiles, wearing apparel and footwear sector. Importantly, this would not mean that the sector is expected to contract in the future, however, as this decrease is relative to the baseline scenario. Instead, a shifting of production away from palm oil and toward manufacturing of clothing and apparel is projected to occur, indicating the greater responsiveness of the Indonesian economy to the removal of trade barriers on the latter.”34

In other words, palm oil production and exports continue to increase (the baseline scenario), but the FTA is likely to promote greater investment in higher-value-added sectors, thus slightly reducing the output of the palm oil sector relative to what would have happened in its absence. These projections did not take into account the likely reduction in imports of palm oil as a result of the phase-out of eligibility for support under the Renewable Energy Directive.

The assessment does not discuss the composition of palm oil exports, but it could be expected that a removal of the import duties on semi-processed and processed products would increase their relative volume as a proportion of total exports (since the import duty rate on crude palm oil is already zero), but that in turn would depend on the extent of investment in processing facilities.

33 - Development Solutions, Sustainability Impact Assessment, Chapter 8.1.
34 - Ibid., p. 178.
2.3 The possible impact of measures similar to those in the EFTA CEPA

Indonesia’s proposals

Indonesia’s proposal for a Trade and Sustainable Development chapter in the FTA, put forward in June 2017, contains extensive language on the treatment of vegetable oils in a dedicated annex, of which the key section is Article 6:

**Article 6: Sustainable vegetable oils standards**

1. The Parties agree that vegetable oils should be produced in a sustainable way.
2. The Parties agree to recognise sustainability standards for sustainable vegetable oil products which have been established by each of Party.
3. The Parties agree that sustainable vegetable products as referred to in paragraph 2 of this Article shall not be subject to any import tariff, duty and/or other charge and to any excise duty or domestic tax imposed by the other Party.
4. The Parties recognise the increased development of sustainability frameworks and standards by non-governmental actors. The Parties recognise the important contribution of such non-governmental sustainability standards to the overall development of sustainability schemes, provided that these non-governmental schemes do not lead to excessive fragmentation, are not anti-competitive, are based on scientific justification and do not mislead consumers.

There are also additional references to the mutual recognition of ‘sustainability criteria and standards applied to vegetable oils that have been independently established by each party’ in the main body of the proposed chapter (Articles XX.11 (2) and XX.12 (3)), and in Article 10 of the Annex, on ‘vegetable oils as biofuels’. In other words, any sustainability standard established by the Indonesian government – such as ISPO – must be recognised by the EU. The third round of negotiations on the FTA, in September 2017, included a presentation by Indonesia of the ISPO scheme.35

On top of this, Article 4 of the Annex, on ‘non-discrimination’, commits the parties to: ‘agree that any internal taxes or charges, as well as laws, regulations and any other measure applicable to the vegetable oils sector, shall be consistent with the respective national treatment or most-favoured-nation obligations enshrined in the General Agreement on Tariffs and Trade (GATT). This would commit the EU to not discriminate against palm oil in trade or through any other measures, as long as palm oil is considered to be a ‘like product’ with other vegetable oils.

Whether vegetable oils are ‘like products’ with each other is debatable. In some ways vegetable oils are highly substitutable for each other (unsurprisingly, as most oilseeds contain the same fatty acids, though in different combinations), being equally usable, for example, as a base for frying, a food additive or a component of biodiesel. In other ways, however, they are different: palm oil tends to be much more energy-dense than other vegetable oils (one reason why it is such a successful crop), and it grows in different conditions and, usually, different countries. Vegetable oils also possess different tariff classifications under the Harmonised System of customs codes; and in the EU, since December 2014, it must be identified individually on food labels (rather than being covered by the generic term ‘vegetable oil’).

The success of Greenpeace’s campaign in 2010 against Nestlé’s use of palm oil in the manufacture of Kit Kat bars, and other NGO campaigns aimed at palm oil, suggests that consumers are able to distinguish products made with palm oil – i.e. that the oils are not ‘like’ – but also that they would be happy to accept products made with other vegetable oils – i.e. that they are ‘like’. The WTO treatment of this issue would have to be decided through a dispute case.

The EU’s proposals

The EU published its proposals for a Trade and Sustainable Development chapter in May 2017. The text, which is fairly similar to equivalent chapters in other EU FTAs, is mainly a series of declarations with no specific commitments. There is no reference to vegetable oils, palm oil or biofuels.

The European Commission’s report on the topic in the ninth round of negotiations on the FTA with Indonesia, in June 2020, stated that: ‘Discussions were constructive, although limited progress could be made. Both parties recalled their objective of concluding an ambitious and comprehensive TSD [trade and sustainable development] chapter. Nonetheless, both sides are still apart on the overall conceptual approach for the chapter and its relation to the other parts of the agreement’. The report on the tenth round, in March 2021, was somewhat more positive, though mainly over climate-related rather than broader issues.

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3 Conclusions

3.1 Sustainability differentiation in trade agreements

The provisions for sustainable vegetable oils in the Indonesia–EFTA CEPA were widely hailed as revolutionary: ‘For the first time in history, a regulatory mechanism will be introduced for the promotion of sustainability through trade preferences’, as one observer put it.38

In fact this kind of trade preference has been attempted before, though not in the context of a bilateral agreement. In 1998, the EU incorporated environmental (and labour) clauses in its GSP; countries meeting International Tropical Timber Organisation sustainability standards for timber products were eligible to receive special tariff reductions of about 25 per cent. No country ever applied for these environmental special incentives, however, perhaps mainly due to the low rate of duties already applying to timber and wood products. The bureaucracy involved and the implicit acknowledgement of trade and environment linkages (often undesirable to many developing countries) probably also contributed to the poor uptake.

The EU currently operates a ‘special incentive arrangement for sustainable development and good governance’ (‘GSP+’), for countries classified as vulnerable (i.e. suffering from a lack of economic diversification and insufficient integration within the international trading system) which also adhere to a list of 27 international conventions on human and labour rights, environmental standards and good governance. GSP+ countries can benefit from complete duty suspensions for products across approximately 66 per cent of all EU tariff lines, including sensitive products (a few of them – the poorest – benefit from zero import duties anyway under the EU’s ‘Everything but Arms’ provisions for the least developed countries).

In September 2021 the European Commission published proposals for a new GSP framework for the period 2024–34.39 Among other changes, the new proposal introduced the possibility of withdrawing GSP benefits for serious and systematic violations of the principles of environmental conventions (specifically, eight multilateral environmental agreements, listed in an annex),40 and extended the list of international conventions that GSP+ countries must ratify to include the Paris Agreement on climate change.

Unlike the 1998 GSP clauses, however, both the existing and the proposed GSP provisions deliver general reductions in import duties across the board rather than reductions aimed at particular commodities associated with deforestation or other negative impacts.

The vegetable oil provisions in the Indonesia–EFTA CEPA are the first time such measures have been included in a bilateral trade agreement. As discussed in Section 2, the implications for Indonesian palm oil exports to EFTA countries are insignificant. The much bigger prize would be the inclusion of similar provisions in the Indonesia–EU FTA and the inclusion of the ISPO standard in the list of acceptable means of compliance.

It may be that Indonesia is trying to establish a similar precedent with regard to exports of palm oil to the United Kingdom (UK). In April 2021, in a visit to Indonesia, British Foreign Secretary Dominic Raab noted that the UK’s proposed due diligence legislation (which became law, as part of the Environment Act, in November 2021) would respect Indonesian local laws and therefore, by implication, recognise the ISPO standard.41 (The UK legislation is intended to

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require importers of forest risk commodities – yet to be specified but almost certain to include palm oil – to exercise due diligence for the risk of their being produced through the illegal clearance of forests. The use of certification schemes such as RSPO or ISPO in proving compliance with the requirements is not yet clear.) Raab’s words were met with positive media coverage and a warm response from Indonesian ministers. The UK–Indonesia Joint Trade Review, started in 2018 as a precursor to a trade agreement, concluded three weeks later. The UK is currently attempting to establish a wide range of trade agreements as quickly as possible to replace the lost trade opportunities due to its departure from the EU.

3.2 Potential ways forward

As noted in Section 2, the negotiations on the EU–Indonesia FTA are currently not proceeding well. It seems extremely unlikely that the EU would accept the Indonesian proposal for the text related to palm oil, but it is certainly possible that the EU could accept the general principle of discriminating in trade on the basis of the way in which products are produced, as in the EFTA CEPA, and also that certification schemes could be used as a possible tool to support the demonstration of compliance with the criteria.

Is there a way in which an FTA between the EU and Indonesia could support trade in sustainably produced palm oil? In principle, as in the EFTA CEPA, the agreement could set out the criteria defining the meaning of ‘sustainability’. The criteria included in the EFTA CEPA are a good start, but to ensure positive outcomes for sustainability, the FTA provisions should be subject to careful review through a multi-stakeholder process, including representatives of oil palm farmers, particularly smallholders, local communities and civil society organisations, alongside government and industry.

Some of the terms used in the CEPA criteria, such as ‘primary forests’ and ‘deforestation’, would need to be defined in detail; for example, the protection of secondary as well as primary forests is important, but at present in Indonesia secondary forests can legally be converted to oil palm. In fact a similar debate is about to be held on the Commission’s proposed Regulation on deforestation-free products, published in November 2021, which prohibits the placing on the EU market of commodities produced through deforestation. The definitions in the FTA and the regulation should clearly be the same, but there are, of course, many other aspects of sustainability that would also need to be reflected in the FTA. The EFTA CEPA criteria touch on some of these – for example ‘respecting rights of local and indigenous communities and workers’ – but they would need to be defined carefully. Others can be drawn from the criteria in the Renewable Energy Directive, including, for example, the requirements not to permit palm oil to be sourced from highly biodiverse land, land with high carbon stock, or peatland that was classified as such in 2008.

The Commission could then conduct an assessment of certification schemes against these criteria, similar to that carried out by SECO in Switzerland (and similar to those it already conducts for biofuels). It is clear that the ISPO scheme in its current form (it was most recently revised in 2020) would not be found to satisfy any such assessment, even against the more limited range of criteria in the EFTA CEPA. As a detailed analysis in 2020...
concluded, among other shortcomings, the principles and criteria of the ISPO standard do not adequately accommodate human rights principles, including free, prior and informed consent, and the rights of indigenous peoples; do not clearly regulate the protection of secondary (as well as primary) forests; and do not reference existing legal frameworks such as the primary forests and peatlands moratorium.44 There is no independent monitoring function, procedures for submitting complaints are unclear, there is no requirement for transparency on the certification process, and the consequences of non-compliance are not clear.

However, the ISPO scheme is due for revision in 2024, and as part of FTA negotiations, the EU could offer support in improving its criteria, implementation and monitoring. The recognition of national schemes is in principle desirable, as it would help to promote buy-in from the producer country – as in the FLEGT VPAs – but of course the standards have to be adequate to deliver genuinely sustainable commodities, both in terms of their criteria and their implementation and enforcement.

More broadly, the inclusion in the FTA of elements drawn from the FLEGT VPAs would help to transform the FTA from a narrow agreement focused only on removing barriers to trade to a much broader effort to promote sustainable development. Examples of elements that could be included are commitments on the part of Indonesia to improve governance and law enforcement, to improve transparency and multi-stakeholder input to decision-making, and to establish a robust and independently verifiable traceability scheme; and commitments by the EU to provide capacity-building assistance, including in particular support for smallholder farmers, as well as improved access to the EU market.

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44 For a detailed analysis, see A False Hope? An analysis of the new draft Indonesia Sustainable Palm Oil (ISPO) regulations (Kaoem Telapak and Environmental Investigation Agency, July 2020).
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What can future trade agreements that aim to promote trade in sustainably produced palm oil learn from previous trade negotiations?