



Small Producer Organization (SPO) Development, Strengthening and Resilience

INDONESIA COUNTRY REPORT

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**Roger Bymolt, Geneviève Audet-Bélanger, Gabriela Quiroga,
Marcelo Tyszler**

Acknowledgments

Local Team Indonesia: Marlina Syarifah, Faisal Agam

KIT: Ellen Mangnus, Ingrid Flink, Verena Bitzer



KIT Royal
Tropical
Institute

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1. Executive summary

Research on Small Producer Organization (SPO) development, strengthening and resilience was commissioned by Fairtrade International to the Royal Tropical Institute (KIT) in the Netherlands. The study is a qualitative-led mixed-method six country study (Côte d'Ivoire, India, Indonesia, Kenya, Mexico and Peru). This country report presents the findings from the research in Indonesia.

Nine SPOs were visited in Indonesia during May 2016, all of them 1st Grade SPOs specializing in premium quality 'Gayo Sumatra' Arabica coffee. Geographically, the SPOs were all located in the Gayo mountain area, near Takengon, in northern Sumatra. Focus group discussions were held with leaders and male and female members separately. A total of 27 SPO leaders, 72 male members and 50 female members participated during the course of the research.

The formation of coffee cooperatives in northern Sumatra is a relatively recent phenomenon. The tsunami of December 26th 2004 brought new attention to the area from international development agencies and the government of Indonesia. Soon after, the long-running civil war between the Indonesian government and the Free Aceh Movement finally ended and the coffee sector began to benefit from greater stability, security and government support. New coffee cooperatives began forming, and the first cooperatives became Fairtrade certified in the late 2000s. The researched SPOs can be broadly categorized as 'business-led' and 'farmer-led'. Business-led SPOs were established by existing trading companies and were early movers, whereas farmer-led SPOs were formed by farmers a few years later and were usually found to be of lower capacity and strength than business-led SPOs.

SPO members expressed broad satisfaction with the training and support provided by their SPOs on good agricultural practices and Fairtrade Standard requirements. While some SPO members initially expressed reservations about environmental rules, which restricted farm expansion on marginal lands or involved more farm labour, there is now broad agreement that the Fairtrade rules and regulations promote positive changes in member villages. Marketing services are the main reason why members join an SPO, and they have clearly been able to secure more power to negotiate prices and dictate terms than individual farmers.

SPOs were found to have suitable governance, as per Fairtrade Standard requirements. Elections are held every three years for SPO leaders and delegates, and these are widely perceived to be transparent and democratic. However, SPO executive boards are rarely voted out as leaders often have status within their communities, are well connected in the coffee industry, have considerable experience and networks, and may be owners of the trade and export companies that partner with the SPO. Therefore, electing new board members can risk disrupting the functioning of the SPO. However, members clearly feel they have a voice in the running of the SPO and the use of Fairtrade Premium money, and can freely express their concerns via their delegates.

Business-led SPOs are stronger than farmer-led SPOs, and face different prospects with regard to sustainability and resilience. Business-led SPOs have a strong presence in the sector and are fully integrated in the value chain, performing all processing stages up to export. Large business-led SPOs are also able to generate margins from coffee sales, while smaller farmer-led SPOs struggle to do the same due to the higher costs involved in outsourcing coffee processing. In general, business-led SPOs have strong systems and manage their operations as an established business. Farmer-led SPOs, however, have much weaker systems in place, less infrastructure and equipment, fewer experienced staff, and are constrained from making necessary improvements by a lack of capital and fewer Fairtrade buyers.

Farmer-led SPOs are more vulnerable to various shocks than business-led SPOs. In recent years, a combination of price shocks, poor business decision-making, and questionable ethics by some SPO partners have hit a number of farmer-led SPOs. Shocks weakened some SPOs and constrained the growth of others. Those SPOs that survived, however, gained valuable experience and have since improved their business practices. Some shocks have been unforeseeable, such as a large earthquake in 2013 which severely damaged several SPOs and member villages. The Fairtrade Premium was extremely important for SPOs, enabling them to respond to the emergency and provide support to SPO members at the time.

The strength, sustainability and success of a farmer-led SPO is closely linked to its relationship with processing and trading companies. Trading

companies and exporters have been vital to the growth of most cooperatives because they link SPOs to buyers and export markets, engage in coffee processing, often provide advance payments to SPOs so they can buy coffee from their farmer members, and often pay the initial costs of organic and Fairtrade certification. Most SPOs only have one trading partner that strongly encourages the SPO to trade solely through them. However, this arrangement also carries a risk because sometimes the relationship goes bad. The arrangement made with a single trading partner has also held back some farmer-led SPOs from expanding further. Larger business-led SPOs have particularly strong external relations because the export and trading partners are often owned by members of the SPO executive board, who have direct relationships with international buyers.

Most SPOs, particularly farmer-led SPOs, have difficulties finding new Fairtrade buyers. Few SPOs sell more than 50 percent of their estimated production as Fairtrade, and all would like to increase the share of members' coffee sold as Fairtrade, primarily because of the attractiveness of the Fairtrade Premium. The Fairtrade Premium is a major factor in SPO strengthening because it generates the working capital for SPOs to deliver necessary services to their members, which in turn has a positive impact on livelihoods and communities. The Fairtrade Premium is also the main source of revenue for farmer-led SPOs to strengthen their internal functioning.

Most SPOs had difficulties when first applying for Fairtrade certification. Firstly, information on the Fairtrade Standards are not available in Bahasa, and very few people in the area speak English. Secondly, at the time most SPOs sought certification, the Fairtrade associate was based in Jakarta, which SPOs said restricted contact and support. Thirdly, SPOs were often unwilling to help other SPOs navigate the Fairtrade certification process, partly because they view each other as competition.

SPOs consider the Fairtrade certification and auditing process to be rigorous, but understand that the Fairtrade rules exist to ensure good governance. However, when misunderstandings occur, they wish to be able to ask questions and receive prompt responses. Communications between FLOCERT – the audit and certification body for Fairtrade – and Fairtrade Indonesia are not as smooth as SPOs would like. Several SPOs expressed concerns about the change from European auditors to Indian auditors, including the responsiveness of auditors, occasional missed audits, and cultural sensitivities. SPOs take the audit process extremely seriously because they have seen other SPOs decertified and understand that the strength of the SPO is linked to Fairtrade certification and receiving a Fairtrade Premium.

Based on the findings of the study in Indonesia, we recommend the following areas where Fairtrade can further support strengthening of SPOs:

- Improve linkages between SPOs and potential buyers;
- Consider providing business development support for farmer-led SPOs;
- Translate core Fairtrade documentation from English into local language, i.e., Bahasa;
- Improve communications and responsiveness between SPOs, Fairtrade staff and FLOCERT;
- Identify reputable legal service providers for SPOs in the area; and
- Conduct analysis of suspended and failed SPOs to understand why they could not sustain their business or adhere to the Fairtrade Standards.

2. Introduction

Research on Small Producer Organization (SPO) development, strengthening and resilience was commissioned by Fairtrade International to the Royal Tropical Institute (KIT) in the Netherlands. The objective of the research was to provide insights into processes of development and strengthening of SPOs that are certified by Fairtrade. The research aimed at identifying the conditions, internal and

external, that are necessary for SPO development to be successful, and how Fairtrade can best support and influence those conditions. The study focused on:

1. Collecting baseline data on present organizational strengths and weaknesses;

2. Providing insights into processes for strengthening of SPOs within the Fairtrade system;
3. Making recommendations for how Fairtrade can best support strengthening of SPOs; and
4. Exploring how the development of SPOs can benefit individual members.

This study is a mixed-method six country study carried out in Côte d'Ivoire, India, Indonesia, Kenya, Mexico and Peru (Figure 1). This country report presents the analytical framework and research methodology. The findings from the research in Indonesia are then summarized, followed by recommendations for Fairtrade.

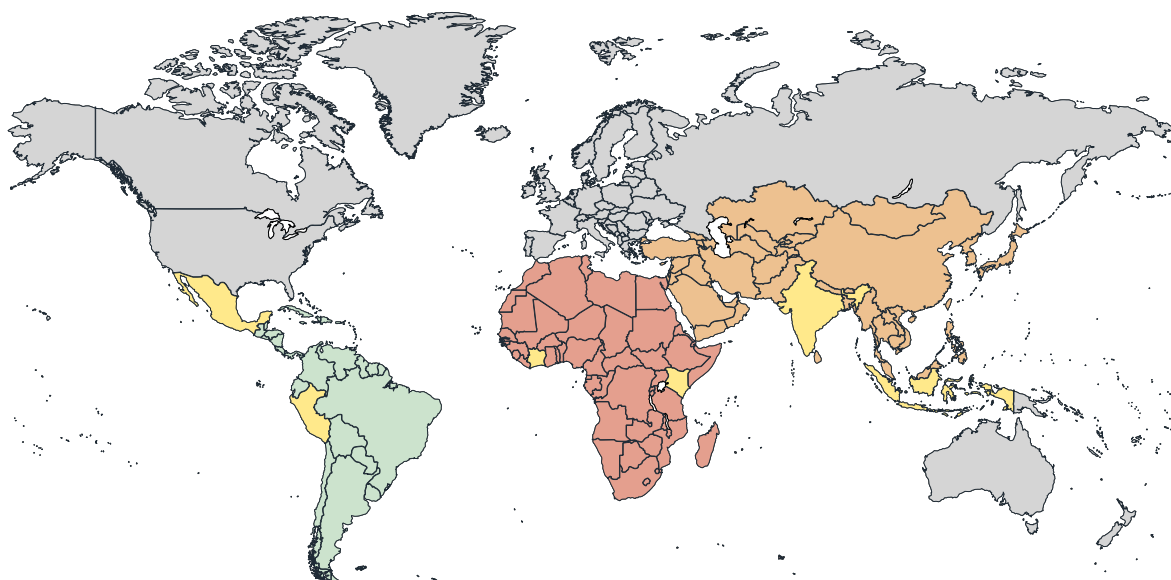


Figure 1. Countries in the study (highlighted in yellow)

3. Analytical framework

Fairtrade articulates a strong SPO as “a sustainable organization with a balanced governance structure, in which democratic principles are practiced and the business is effectively managed based on the collective needs of the members. The above requires for an SPO to have good governance and business management capacities in place, serving a common purpose that is owned and internalized by its members.”¹

Successful SPOs, therefore, must be imbued with the following characteristics:

- Democratic structures to ensure participation and communication;

- Good governance, inclusive leadership and transparent management;
- Skill sets and capacities for managing businesses; and
- Strong economic and financial foundations.

SPOs' access to relevant information, resources and services, and infrastructure is essential. Moreover, organizations must be resilient, i.e., have the ability to anticipate, prepare for, and respond and adapt to incremental change and sudden disruptions to survive and prosper.

¹ Fairtrade International (2013). *Fairtrade Theory of Change*, December 2013

Baser and Morgan (2008)² developed a 'five core capabilities framework' to assess an organization's capacity and resilience. The five interrelated capabilities (5Cs) are:

1. The capability to adapt and self-renew;
2. The capability to act and commit;
3. The capability to relate to external stakeholders;
4. The capability to achieve coherence; and
5. The capability to deliver on development objectives.

1. **The capability to adapt and self-renew** is key to the resilience of an SPO. It requires reflexivity, i.e., the capacity to affect and interact with the environment in which the organization and its members operate. This, in turn, needs a certain level of flexibility, which can be a challenge for SPOs. The capability to adapt and self-renew requires good leadership and strong adaptive management capacities with a clear mandate and the autonomy required to take and implement decisions if necessary. Democratic structures, inherent to SPOs, can sometimes hamper flexibility. At the same time, ownership by, and accountability to members, and consequent communication and information provision, are seen as key qualities of an SPO. In addition, many SPOs are bound by arrangements with their donor organizations or traders, or at least perceive their relationship with donors as restricting.

2. **The capability to act and commit** is related to the individual capacities of an SPO's leaders, staff and members to fulfil their roles and perform these according to agreed standards. At the same time, this capability refers to the degree of management and leadership autonomy to take and implement decisions if needed (see the capability to adapt and self-renew). The capability to act and commit also depends on the systems and structures in place, which determine the space that leadership and management have to operate freely. Again, this requires balancing democratic principles, accountability and transparency on the one hand and the ability and flexibility to respond adequately and in a timely manner to emerging challenges on the other.

3. **The capability to relate to external stakeholders** is embedded in the nature of SPOs as they develop and maintain linkages with external actors (which

may include private sector value chain actors, service providers or public sector and government agencies) on behalf of their members. These roles include policy influencing, lobbying and advocacy, mobilizing support, and negotiating better services and a better position in the value chain. The interactions can result in improved access to services, improved policies, rules and regulations, access to markets and more power through improved value chain linkages, among others. However, there seems to be a general tendency among SPOs to switch between actors rather than to maintain and enhance relationships. SPOs are also prone to taking up certain value chain functions that can sometimes be more effectively carried out by other actors. For example, rather than negotiating better arrangements with traders, SPOs engage in trading themselves. It is important that SPOs are truly representative of their members in order to be considered credible partners by stakeholders, and to ensure that the benefits of improved external relations serve the majority of their members.

4. **The capability to achieve coherence:** SPOs represent a multitude of farmers: large, small, marginal, men and women, young and old, subsistence and/or market oriented. The needs, interests and ambitions of these farmers vary greatly. Many organizations struggle to truly represent this diversity. Who are the members? Whose agendas dominate? Is the organization inclusive? Can it be really inclusive? Are women's interests sufficiently addressed? And what structures and systems are in place to allow this? Setting objectives and translating these into services that meet the needs of all members is a significant challenge for most SPOs. SPOs are supposed to be guided by democratic principles, but these may not always avoid bias and exclusion. If members do not feel represented they might lose interest in and loyalty to their organization. Business-oriented organizations face risks particularly if members' loyalty is at stake. For example, agreed deals or contracts need to be respected, but if members decide to supply other markets the organization will fail to meet its contractual obligations, affecting other members and the organization itself.

5. **The capability to deliver on development objectives** is partly related to resources, both human and financial. The organization can mobilize and commit to its activities,

2 Baser, H. & P. Morgan (2008). *Capacity, Change and Performance Study Report*. European Centre for Development Policy Management, Discussion Paper No. 59B, April 2008

but its capacity is also influenced by the systems and procedures in place such as: administration, finance, information management, monitoring and

evaluation (M&E), communication, and the facilities available (hardware).

4. Research methodology

The study used a qualitative-led mixed-method approach to research in order to ensure research validity, reliability and rigour. The analytical framework previously described, in combination with a grounded-theory approach, provided guidance to researchers during the fieldwork in the six countries. These tools allowed the primary qualitative data to be analysed, and the main conclusions and recommendations to be drawn.

4.1 ANALYTICAL LENS FOR THIS STUDY

In order to understand the underlying factors and conditions that contribute to making a strong SPO, and how Fairtrade can better support these organizations, an analytical lens has been used. Based on the 5Cs framework and Fairtrade definitions presented above, a desk review and further discussions with Fairtrade were conducted to analyse the strengths and weaknesses of SPOs for this study:

- Services to members:

An essential function of a strong SPO is to provide services to its members, and how this provision evolves over time is a key factor in its success. We investigated which kinds of services are provided, such as training, provision of inputs and equipment, financing, transport, storage, processing and marketing of produce, and advocacy and lobbying, as well as the level of member satisfaction with these services. Where possible, we provide evidence of members' satisfaction and commitment towards their organization.

- Governance and management:

A strong SPO requires a balanced governance structure and good management. We investigated leadership structures and elections, decision-making processes and communication flows within the SPOs.

- Sustainability and resilience:

A strong SPO needs to be economically and environmentally sustainable and ready to adapt,

react and renew. We investigated the levels of (and variation in) production and sales, shares of Fairtrade sales, and how vulnerable the SPO is to local and system shocks (e.g. climate change) and trends (including risk mitigation measures).

- Business practices:

A strong SPO has effective and transparent internal business management and is in control of its business relations including negotiating power, access to markets and finance, and strategic and business planning capacity. Additionally, it is capable of controlling quality during production practices. We also investigated how business is carried out with partners in the supply chain.

- External relations and partnerships:

A strong SPO also engages with local and/or national government and other organizations for the benefit of its members. We investigated if such relations exist, how other stakeholders are involved, what these relations are for, as well as how they evolve and develop over time.

Within each aspect listed above, we analysed the following issues:

- Overall findings: what are the overall findings and are there any particularly informative deviations?

- Crop specific particularities: are there any particularities which apply to one commodity but not others?

- Contrast leaders vs members: are member views in line with the leadership?

- Contrast men vs women members: do men smallholder farmers have similar views to women smallholder farmers?

- Variation according to membership size: does membership size influence the function and strategy of the SPO?

- Variation according to age of SPO: are there any relevant variations according to the age of the SPO?

• Variation according to time of certification: how does the length of time an SPO has been certified influence organizational strengthening?

4.2 TECHNIQUES FOR DATA COLLECTION

Primary data collection relied on qualitative interviews generated from:

1. Semi-structured focus group discussions (FGDs) with SPO leadership and management;
2. Semi-structured FGDs with men members;
3. Semi-structured FGDs with women members; and
4. Key informant interviews with local representatives from Producer Networks and local Fairtrade staff.

Primary data was complemented with secondary data about the SPOs, and was made available by Fairtrade in the form of audit and closing reports, FLOCERT³ checklists and non-conformities files.

4.3 COUNTRY SELECTION

The research aimed at capturing a diverse geographical range, based on the countries with most Fairtrade certified SPOs. KIT, in collaboration with Fairtrade, chose six countries covering three geographical areas: Latin America (Mexico and Peru), Africa (Côte d'Ivoire and Kenya), and Asia (India and Indonesia).

4.4 SELECTION OF SMALL PRODUCER ORGANIZATIONS (SPOS) IN EACH COUNTRY

In each country, ten SPOs were selected for visits. The majority were 1st Grade SPOs (members are individuals, often smallholder farmers) and at least one SPO was 2nd Grade (an association of farmer organizations). Pre-selection was proposed by the local Fairtrade Producer Network and a final selection was made maximizing variability in indicators such as the age of the SPO, years of certification, crops, men/women in leadership roles, number of members, and presence of professional staff.

The sample of ten SPOs per country was found to be enough to reach an acceptable level of saturation, i.e., a point in qualitative grounded-theory research in which additional sampling will not lead to significant expansion of the analytical categories, but is sufficient to provide enough confidence to the researchers that the main issues are being captured.

4.5 SELECTION OF FOCUS GROUP DISCUSSIONS (FGD) PARTICIPANTS

Research participants needed to be SPO members, or a member of a household where one person is a member or employee of an SPO.

Elected board members and professional staff were invited to the FGDs with the leaders and managers. The selection of participants in the qualitative interviews was as random as possible, with a maximum number of participants to allow for quality discussions.

As a qualitative data collection tool, focus group size does not require power calculations, since statistical significance is not its main goal. Yet, for reference, we can show that for incidence questions (yes/no, binary questions), 43 observations were enough to estimate percentages with a 15 percent error margin and a 95 percent confidence interval. In each SPO, we aimed to consult 40 people in total from the three different types of FGDs (leadership and management, male members, female members).

4.6 VISITS IN INDONESIA

Nine SPOs were visited in Indonesia, all of which were 1st Grade coffee SPOs. Geographically, the SPOs were all located in the Gayo mountain area, near Takengon, in northern Sumatra. FGDs were held with leaders and male and female members separately, except in one case where there were very few female members.

The visits took place during May 2016 and a total of 27 leaders, 72 male members and 50 female members were interviewed.

Due to confidentiality requirements, the SPOs that participated in the research are not named in this report. Instead, codes have been used to denote SPOs, such as 'SPO-5'.

³ FLOCERT is a global certification and verification body. Its main role is to independently certify Fairtrade products. Accessed 04-01-2017 <http://www.flocert.net/>

5. Analysis of SPOs strengths and weaknesses

5.1 INTRODUCTION AND CONTEXT

The formation of coffee cooperatives in northern Sumatra is a relatively recent phenomenon and is the outcome of several contextual factors. The people of Aceh suffered through a long civil war between 1976 and 2005, involving the Free Aceh Movement (GAM) and the Indonesian government. On 26th December 2004 a powerful tsunami devastated Banda Aceh, resulting in a humanitarian crisis which led to an influx of support from the Indonesian government, humanitarian agencies, and later, various development agencies and non-governmental organizations. In the aftermath of the tsunami, GAM declared a unilateral cease-fire, with members of the international community reiterating the need to resolve the conflict. Although earlier peace efforts had failed, a peace agreement was finally reached in 2005 after 29 years of war.

The coffee sector benefitted from the greater stability, security and government support which dramatically improved the business environment in the region. The earliest cooperatives in the research sample were formed around 2007. Several interviewees recalled how interest in forming a coffee cooperative could also be traced to what is known locally as the 'Holland Company'. While interviewees could not recall the precise details of the company, one described it as an Indonesian state-owned coffee trading company that had a strong relationship with a Dutch company. The colloquial name 'Holland Company' comes from the fact that many Dutch businessmen came to the area and worked with the coffee trading company.

SPO-4 was one of the earliest coffee cooperatives to be formed in early 2007. However, it soon came under intense pressure from local coffee collectors working for traders. In 2007, the local collectors

turned against the cooperative and attempted to persuade local politicians to close it down because they were struggling to compete with the prices the SPO was paying its members for certified organic coffee. The cooperative chairman entered into negotiations with local politicians and reminded them that the number of potential voters who were SPO members exceeded the number of local collectors. Through negotiation, the SPO was able to convince the government that they were contributing to the local government's economic strategy. The cooperative helped rebrand the area's coffee from 'Sumatra Mandailing' to 'Gayo Sumatra' to distinguish its particular characteristics and quality. The cooperative also explained to the government that it had been transparent and compliant with the law.

The outcome was positive and the local government supported the cooperative, and other traders and agents began to establish their own cooperatives to compete with SPO-4. This helped to drive growth in coffee production and establish the reputation of the Gayo brand to the extent that all coffee from the area now bears this name. The example of SPO-4 highlights how SPO leaders need to be savvy if they are to challenge the status quo and navigate a challenging political landscape. SPO-4's leader was experienced, educated and motivated, and frequently attended local government meetings to build relationships with influential people.

5.1.1 Business-led cooperatives

The earliest cooperatives in the sample (formed in the late 2000s) can be considered 'business-led', as they were all led by business owners of export trading companies (PTs and CVs⁴). They possessed several characteristics that helped them to be successful almost immediately, including:

4 PTs and CVs are forms of privately-owned companies in Indonesia: *Commanditaire Vennootschap* (CV), and *company limited Perseroan Terbatas* (PT). The CV is an enterprise that is established by two or more persons as partners, either active partners or silent partners. Active partners are those that provide capital as well as run the business, while silent partners are those who provide venture capital. Active partners have full responsibility for all the company assets and liabilities, and silent partners are responsible only for the capital paid.

A PT is a business entity whose capital is divided into stocks (shares). The responsibility for liabilities/debt for the company is limited to the owners of holdings. There are two types of limited companies, namely a closed PT and an open PT. A closed PT is one whose shareholders are limited, for example among families. An open PT (often called PT going public) is a PT whose common shares are sold to the public. For more information see: <http://www.cekindo.com/indonesian-business-entities.html> and http://www.ssek.com/download/document/Establishing_a_Business_in_Indonesia_106.pdf

international business experience in coffee trading through the Holland Company, existing business relationships, an entrepreneurial attitude and an appetite for risk, access to capital, and – in a number of cases – the use of processing, warehouse and office facilities.

The trading companies were already operating informally in villages across the district and procuring from smallholder coffee farmers on an *ad hoc* basis. The traders identified an opportunity to grow their coffee processing and export businesses by organizing the farmers they were already working with. They assumed, correctly, that the farmers would be open to organization because it would help them realize higher prices and generate more demand for their coffee. Forming early was an advantage for cooperatives. They faced little competition and were able to gain new members easily as most coffee farmers were unorganized and unaffiliated.

SPO-4's strong position in today's market stems from its leader's strong prior experience in the sector, coupled with support from institutional partners. It began as a savings and loans cooperative, led by five entrepreneurs who each invested 1,000,000 Indonesian rupees (IDR; approximately €70). One of the original founders is the current chairman. SPO-4's executive board explained how important the experience of operating a microfinance institution had been in developing current business management practices. In addition, members of the current executive board also managed their own small coffee trading companies (CVs) so had a good understanding of the industry. After the tsunami and the end of the conflict in 2005, SPO-4 was able to harness support from the United States Agency for International Development (USAID) via the National Cooperative Business Association (NCBA), which had a project to rehabilitate coffee farms. With the support of NCBA, the SPO was able to export a few containers of coffee to the US. Business went well, and SPO-4 gained further support to become certified organic and register its members.

Another example of a business-led cooperative is SPO-6. Formed from a family trading company that had a long history in the coffee industry, SPO-6 possessed all of the necessary ingredients for success from its inception. A strong business network and existing facilities all provided SPO-6 with the best possible start when it registered as a cooperative in 2009. To improve business for themselves and farmers in their community, the leaders of SPO-6 formalized coffee farmers under a cooperative structure to supply their existing

processing and trading business. Small traders who had already worked with the trading company were offered roles as coffee 'collectors' under the cooperative structure, so there would not be any disruptions to supply. The founders of SPO-6 remain on the executive board, and have grown both the SPO and their private coffee processing and export business into some of the most successful ventures in the area.

SPO-7 is another example of a business-led SPO, which was formed by a local trader/exporter who had been procuring coffee from farmers for a number of years, and saw the demand for organic and certified coffee plantations. Creating an SPO enabled the exporter to expand and grow his processing and export business, while at the same time realizing higher prices for farmers.

5.1.2 Farmer-led cooperatives

Although farmer-led SPOs have enjoyed a degree of success, their business growth trajectory in terms of volume growth has typically been much flatter than business-led SPOs, both because they began later and because they lacked the experience, knowledge, networks, facilities and capital of business-led SPOs. Prior to formally becoming cooperatives, SPO-1 and SPO-5 began as small groups of farmers coming together in the hope that, by organizing themselves, they could have more power in negotiations with buyers on prices and volumes. Formalizing as a group was thought to be a way to maintain good prices during peak harvest times, and improve transparency in how prices were established. Farmer-led cooperatives were often led by champion farmers – with extensive farming experience, knowledge and skills, which they have diffused to other farmers – and not necessarily by those with strong business or organizational experience, networks and connections, or existing processing facilities.

5.2 CAPABILITY TO ADAPT AND SELF-RENEW

5.2.1 Organic certification

All of the interviewed SPOs sought organic certification in some form shortly after their formation as a cooperative. Some were strongly encouraged to do so by trader/exporters, who were increasingly aware of the growing demand for organic coffee in America and Europe.

The leaders of business-led cooperatives saw them as an extension of their private export and processing businesses, and were thus vested in the

cooperative's growth. Farmer-led cooperatives on the other hand were more dependent on a good relationship with a trader/exporter.

In most cases, the trader/exporter paid for and owned the organic certification, allowing the SPO to grow rapidly. Farmer members did not see this as a problem initially because organic certification was perceived to be expensive (around €7,500) and farmer-led SPOs lacked start-up capital to finance this. Furthermore, farmer members were satisfied with the arrangement because they expected the organic certification to help them to realize higher prices, which was their main interest.

This arrangement, however, often came with the condition that the SPO would exclusively supply the trader/exporter. For most cooperatives, an exclusive supply arrangement helped them to establish and grow their membership base relatively quickly. However, this arrangement also had the potential to block SPO strengthening in the long term because it discouraged SPOs from finding new buyers and exporters, and the fate of an SPO is closely tied to the success or failure of export business.

5.2.2 Price shocks

SPOs that had initial success delivering small Fairtrade consignments said that they felt empowered to sign larger contracts. However, several farmer-led SPOs in the sample experienced major price shock events which threatened their sustainability, and a lack of business experience contributed to poor decision-making. These SPOs made the mistake of signing sizable contracts with long future delivery dates without understanding price risks. Despite fairly stable prices in the 2010 season, local prices were said to have increased by more than 50 percent during the 2011 season. This meant that several SPOs could not afford to buy coffee from their farmer members and were left with two hard choices – to deliver on the contract and suffer big losses, or default on the contract and face consequences such as legal action, losing a buyer or trading partner, or even losing Fairtrade certification. When such situations occur, it is important that SPOs have access to advice and legal support they can trust. Most SPOs tried to struggle through the situation alone.

Business experience and being able to understand risk on a global level is vital to the sustainability of an SPO. SPO-3, for example, signed a one year forward contract with a fixed price in 2011. When

world market prices spiked, the SPO was left facing a €90,000 loss. The executive members said that exporters told them this was normal practice but the SPO did not foresee the shock, which was caused by a long dry season in Brazil (the world's largest coffee producer) that affected world prices. SPO-3 now only signs contracts for one lot at a time.

Most SPOs who found themselves in similar situations tried to enter into negotiations with the buyer to delay delivery, or partially deliver on the agreement, knowing that technically, they would be in breach of the terms of the contract. However, some SPOs described how they had had considerable difficulties contacting buyers to explain their situation because their trading partners withheld contact details. This was possibly to ensure that the SPO could not deal directly with the buyer and cut out the exporter.

Buyers who were eventually contacted responded in various ways – some were flexible and others were strict with contractual terms. Some SPOs received legal notifications from buyers, and also from their exporting partners, and some even experienced threats and manipulation. More than one SPO was dropped by its trading partner as a result of the process as they shared liability. SPO-2 lost half of its members to its former trading partner as a result.

One SPO allegedly received warnings from FLOCERT⁵ that they would lose their certification if the pending contract was not fulfilled. The SPO in question said that they did not know where to turn because it was very difficult to get access to Fairtrade to explain their situation or receive reliable advice.

Major negative events such as price shocks have resulted in SPO board members resigning, requiring new board members to be appointed at short notice. However, SPOs described the difficulty in finding new leaders with the capacity and management experience to adequately deal with the problems SPOs face. Furthermore, members were wary of taking on the risk and responsibility of managing an SPO facing major difficulties. Fairtrade should be aware that, in crisis situations, new SPO leaders are likely to require additional support if the SPO is going to successfully recover.

5.2.3 Natural disasters

In July 2013, a major earthquake struck the area, causing severe damage to SPO buildings and

5 FLO-Cert is the inspection and certification body for Fairtrade products.

office equipment. Farming communities were also greatly affected. SPOs responded by supporting their members through emergency relief and food provisions. Affected SPOs described the earthquake as a great setback to their short and medium term plans. However, they stressed that Fairtrade Premium money had improved the SPO's resilience and enabled them to support their members during this difficult time.

5.2.4 Computer systems

Many SPOs, particularly farmer-led SPOs, do not have much IT expertise so basic support on good IT practices would improve their resilience by averting future system failures. Several SPOs have suffered from viruses or hard drive failures, resulting in massive SPO data losses. While most SPOs have hard copies of annual reports and financial data, they often have no reliable backup system (external drive, server, cloud server, etc.), and only have files on a single computer.

5.2.5 Learning from failed SPOs

Interviewees reported that approximately five SPOs in the area were decertified between 2011 and 2013. While the SPOs interviewed were able to struggle through when the price crisis struck, several SPOs took poor management decisions. Some researched SPOs recalled stories of other SPO executive boards trying to use Fairtrade Premium money to service debts without following Fairtrade regulations, or gaining approval of members. An exporter and SPO chairman also allegedly shipped low-grade coffee to a buyer and sold the high-grade coffee on the local market to realize greater profits from the price spike. The exporter and chairman allegedly fled the area. This shows that SPO strength, and sometimes survival, very much depends on good leadership and decision-making by the executive board. In practice, this means being strategic, honest and ethical, and having the capacity to navigate and negotiate difficult circumstances.

Other SPOs were said to have been deregistered due to Fairtrade non-compliance, such as being unable to provide the necessary traceability documents. Interviewees suggested that while the Fairtrade rules were breached by those SPOs, there may have been a lack of awareness about these rules, rather than an attempt to mislead. If so, it may be an indication that SPOs require more training concerning their obligations to provide documentation and traceability data.

5.3 CAPABILITY TO ACT AND COMMIT

Business-led SPOs clearly have strong systems and manage their operations as an established business. Farmer-led SPOs, however, have much weaker systems in place, less experienced staff, and are capital-constrained from making necessary improvements. The financial reports of farmer-led SPOs showed that most of the executive members and managers receive little more than the minimum cooperative wage in Indonesia.

5.3.1 The process for assessing a contract

SPO-7 described how they consult with members, via delegates, when considering a new contract. The leaders communicate to members the essential details of the contract and if 80 percent agree to the terms, the SPO will sign the contract. However, in reality, the SPO found that when local prices increase in the intervening period, members refuse to sell their coffee for less than local spot prices. This appears to be a particular problem for nascent SPOs whose members do not fully understand the Fairtrade system, are interested in short-term gains, and have yet to establish strong solidarity with the SPO. When the SPO is forced to increase the price to its farmer members after signing a contract, it generates a loss for the SPO. SPO-7 explained how in one particular year they received €90,000 in Fairtrade Premium money but incurred trading losses of €11,000. At the annual general meeting, SPO-7 needed to request authorization from members to cover the trading losses from Premium funds, and remind members of their obligations.

When SPOs negotiate a contract, they must also factor in processing costs to turn cherry into green beans (green asalan). The processing stages obviously incur costs – a collector is paid around 150 IDR/kg (approximately €0.01/kg) excluding pulping, or 2,600 IDR/kg (approximately €0.175/kg) for all processing costs. The SPO must also factor in a small margin of around 1,000 IDR/kg (approximately €0.07/kg). It is clear that some of the smaller, farmer-led SPOs, do not have sufficiently accurate tools for estimating all costs and margins. This can lead to unexpected losses or smaller profits than planned. Fairtrade or other partners could contribute to the development of a simple Excel spreadsheet for all SPOs to help them calculate costs and profits more accurately.

The decision-making processes of an SPO can also be negatively affected by pressure from farmer members. For example, SPO-7 described how since forming, their main concern has been to keep

skeptical farmer members happy and maintain their membership numbers. To do so, the SPO decided to buy all the coffee farmer members produced, regardless of whether or not they had a contract with a buyer. SPO-7 leaders used the local price as a guide, but conceded that this sometimes rose higher than the Fairtrade Minimum price. This is clearly a dangerous strategy, leaving SPOs exposed to drops in global market prices.

5.3.2 Prices

SPOs consider there to be a high demand internationally for organic Gayo coffee; this perceived high demand increases local prices – which can often be higher than the Fairtrade Minimum Price (which is a floor price to protect farmers – higher prices would depend on negotiations with market partners). SPO-9 notes that while local prices may be a few percent higher than the Fairtrade Minimum Price, the SPO always pays its members promptly, whereas small traders pay after they have sold the produce. When farmers agree to sell to traders, most of the time, traders pay farmers only after they have sold the produce. Therefore, when selling to traders, farmers carry the risk that the trader will disappear without making the payment.

Some exporting SPOs, such as SPO-6 have affiliated themselves with the Indonesian Coffee Exporters Association which provide regular price updates, including from the Indonesian Ministry of Trade. This helps the SPOs have a better understanding of prices because some exporting companies do not always reveal information about price movements.

Successful business-led SPOs, such as SPO-6, described the coffee sector as “full of tactics”, where price negotiation is “a kind of game”. SPO-6 says that an SPO must monitor the local and international price dynamics very closely and be willing to say no to some contracts. However, declining contracts is probably a luxury that only large business-led SPOs have because most farmer-led SPOs have difficulty accessing new Fairtrade buyers.

5.3.3 Unethical business practices

When an SPO is not run by an experienced board with a good understanding of business and legal issues, they can quickly find themselves out of their depth when serious challenges occur. Farmer-led SPOs in particular are very risk adverse and when problems occur, they do not always seek help to resolve them. For SPO-3, the unethical business practices of an exporter greatly affected the functioning and sustainability of the SPO. In 2010, an exporter only

passed on 25 percent of the Fairtrade Premium owed to SPO-3. The SPO leaders met the exporter and, after negotiations, the exporter agreed to pay the outstanding Premium in instalments. The SPO leaders took a ‘personal approach’ because they wanted to maintain the relationship with the exporter. However, Premium money was again withheld in 2011. While some instalments were paid, payments were not completed.

During the annual FLOCERT audit, SPO-3 was issued with a warning to follow-up with the exporter and their members. At the AGM, it was agreed to seek legal advice, and if the situation did not improve, to end the contract with the exporter. However, SPO-3 continued to sell to the exporter and actually increased the size of its contracted volumes because they did not want to lose their members to rival SPOs and it was the exporter who held the organic certification. SPO-3 contacted a lawyer when the exporter withheld their Fairtrade Premium for a third year in a row. Unbeknownst to the SPO, the exporter allegedly forged letters stating that the SPO agreed to delay the Premium payments. During the next annual audit, the forged letters were presented and used by the exporter to try to avoid repaying the SPO. However, with assistance from the lawyer, the exporter began repaying the Premium monies in large instalments, although €42,000 remains outstanding. Members decided against suing the exporter because it would cost them money to take him to court and there was a lack of trust towards the justice system. As a result, SPO executives had to personally take loans from friends in order to cover the running costs of the SPO, and its membership fell from 1,500 to around 650 members.

SPO-3 says that they attempted to contact FLOCERT and they reported the situation to Fairtrade Indonesia who essentially advised them to mediate, which the SPO felt would not be successful. Despite reporting the problem to both bodies, no action has been taken against the exporter, who is still operating. It should be noted here though that this reflects only the SPO view, as interviewing exporters was beyond the scope of this study.

5.4 CAPABILITY TO RELATE TO EXTERNAL STAKEHOLDERS

The success of SPOs is closely intertwined with the support they receive from their trading partners. Exporters have been vital to the growth of most cooperatives, because they link SPOs to buyers and export markets. They often pay for the organic and Fairtrade certification on behalf of the SPO, perform

part of the coffee processing, and provide advance payments to SPOs to buy coffee from their farmer members. Most farmer-led SPOs have only one or two trading/exporting companies with which they partner. While this is a risk, they often do not have much choice and new buyers – particularly good, honest partners – appear to be difficult to find.

Several SPOs do have good relations with their trading company and cite them as a reason for their stability. Unfortunately, other interviewed SPOs had seen good relationships go sour, usually due to the trader or exporter engaging in unethical behaviour in the viewpoint of the SPO.

Prior to the formation of coffee cooperatives, traders and exporters organized farmers and paid for organic certification. Hence, most of the farmer-led SPOs are bound to traders and exporters who hold their organic certification. SPOs cannot apply for organic certification with the same farmers who willingly certified years earlier. Although a large number of members could renounce their certification, this seems unlikely. Individuals do not want to take this risk, the SPO would have to pay to re-certify, the process could take quite some time, and the SPO would almost certainly lose their relationship with the exporter and buyers. Weaker SPOs therefore reported feeling 'stuck' or 'restricted' and SPO leaders say they are careful to keep the CVs and PTs4 onside to avoid risking the relationship that allows them to sell organic coffee overseas.

Where a relationship with a trader or exporter has gone wrong, SPOs believe there is little recourse to the law, that lawyers cannot be trusted because they can be paid off, and that the costs and time involved in seeking justice can be prohibitive. After the price crunch in 2011, for example, a new executive board required support and took up an offer of assistance from a businessman, exporter and former chairman. The businessman offered to sell a warehouse to the SPO at an inflated cost. Furthermore, until the SPO could raise the full capital to make the purchase, the SPO agreed to rent the premises. In return, the businessman promised to introduce the SPO to new buyers and exporters – but neither materialized. Then, knowing that an audit was due, the businessman allegedly demanded an additional payment, without which, he threatened to lock the SPO out of the warehouse, which could see it fail its audit. The SPO chose to make the extra payment. This is an example of an unfortunate effect of auditing which led an SPO to make a bad business decision.

5.4.1 Processing and export partnerships

Trading and export companies often carry out all of the processing stages for farmer-led SPOs (hulling, drying, grading etc.). Trading companies are happy to do so because they are efficient, have the facilities, and can make an additional margin. Small SPOs find it challenging to process and export produce themselves, whereas business-led SPOs have the requisite market linkages, expertise and facilities to undertake processing and marketing activities. Among the SPOs interviewed, only two were exporting their produce directly. They had the support of their executive board members who own processing and export companies.

5.4.2 Links with buyers

Most SPOs do relatively little to market themselves internationally, and appear to need assistance in this area. For example, very few have a website, or even a Facebook page to promote their coffee and that of the area. Yet, even if they did have these platforms, they would need assistance in promoting themselves online and would need the website to be written (and updated) in English. One suggestion from SPOs was for Fairtrade to have a page on their website for SPOs, so that buyers could find them and their contact details.

Access to good, reliable buyers of Fairtrade coffee is the single most important issue for SPO strengthening. SPO-6 highlighted the importance of promotional events and conferences outside their country where they can come into contact with new buyers. SPOs who have been to such events say that these invitations mainly come from Fairtrade USA. All SPOs are looking for new buyers and have a lot of difficulty – either buyers are interested but cannot find them, or there is a lack of demand. SPOs believe that there is demand, and that more could be done by Fairtrade to promote Fairtrade SPOs in international markets.

5.4.3 Financial partners

Farmer-led SPOs have often needed to borrow money from executive board members to make basic investments. However, for SPOs involved in processing and export, access to revolving credit is particularly important. SPO-6 performs all processing stages, using facilities owned by the chairperson, and has a successful track record. Their success has brought them into contact with Root Capital – a non-profit social investment fund operating in poor rural areas of Africa and Latin America – from whom they can now borrow €930,000 from a revolving fund. This has led other SPOs to wonder if Fairtrade would be able to bring

them into contact with other investors such as Rabobank. Essentially, farmer-led SPOs do not know how to engage institutional investors and this is a new consideration for many.

SPOs generally do not offer savings and loans facilities, and hence do not require a financial partner to support such a service.

5.5 CAPABILITY TO ACHIEVE COHERENCE

Fairtrade has had a positive influence on governance among researched SPOs. All SPOs in the sample were registered under Indonesian cooperative law prior to becoming Fairtrade SPOs, and remain so today, but prior to Fairtrade certification there was no delegate system, and elections were generally not held regularly. Now, communication flows are much improved between members and SPO leadership thanks to the delegate system. SPOs hold elections every three years, and leaders and members alike perceive these to be transparent and democratic. Elections are a Fairtrade requirement and are held for executive board roles, including chairperson, treasurer and secretary. Each member is able to cast one paper vote in a secret ballot box so that people cannot identify how members vote.

There is little turnover of SPO executive boards for several reasons. Executive board members tend to be founding members of the SPO, who have committed considerable personal effort and even financing towards the establishment of the SPO, and so are afforded a certain status in the community. Furthermore, founding SPO leaders usually know the coffee business better than other members. Provided the SPO is performing satisfactorily, members seem not to be interested in voting for new board members. Farmer members also generally believe that founding board members are the best at managing the business, and value their important business relationships with traders and buyers. Electing a new board could therefore disrupt business relationships.

Business-led SPOs are also often successful because they utilize the facilities and expertise of 'sister' processing and trading companies, which may be owned by SPO executive board members. Business-led SPOs often get favorable terms from sister processing companies, and are well linked to buyers via sister trading companies. Some business-led SPOs are so intertwined with these trading and processing companies that they share the same warehousing and office space.

If farmer members were to vote out the executive board, the SPO may lose access to these facilities, networks, and buyers.

Voting for delegates works in much the same way as voting for the executive board. Delegates are smallholder farmer members who act as intermediaries between members and the board. Delegates give a voice to the concerns of farmer members in meetings and assemblies, and also bring information from the board to the members so they are sufficiently aware of management decisions. This is particularly important for the AGM because SPOs cannot logistically host thousands of members at one location. Most SPOs in the sample have a ratio of 1:30 or 1:50 delegates to members.

During FGDs, members made it clear that they feel they have a voice in how the SPO operates. Members frequently said that they can freely express their concerns, and via their delegates, systems are in place for constant and effective communication. SPO board, members and delegates were all overwhelmingly supportive of the delegate system. However, while members expressed broad satisfaction with how their cooperatives were run, they typically did not know much about how the SPO functioned, nor did they express much interest in management issues. Members' main concerns were simply to sell as much Fairtrade coffee as possible in order to generate the greatest amount of Fairtrade Premium, and to sell their remaining coffee for the best price they could.

5.5.1 The Fairtrade Premium

The Fairtrade Premium helps to increase the social cohesion of members to their SPOs, because it allows SPOs to deliver goods and services that members need and desire. Members are very positive about the Fairtrade Premium and, at all of the visited SPOs, they voted on how they would like to spend Premium receipts. This is then communicated to the leaders through the delegates. The most frequent requests by members were for grass cutting machines and other equipment, clothes, and gifts of food during religious celebrations. The Premium is also used to train members via the Internal Control System (ICS), to ensure that they continue to comply with the Fairtrade Standards.

For farmer-led SPOs, the Fairtrade Premium is essential for growth, strength and sustainability because they often struggle to generate margins in the face of stiff competition from larger competitors. As farmer-led SPOs do not process the beans themselves for export, they incur higher external processing costs and create lower margins

than large business-led SPOs. Therefore, while efficient business-led SPOs may be able to make a small margin per kg, farmer-led SPOs struggle to do the same.

5.5.2 Limitations on SPO growth

There are now few villages in the Gayo area that do not benefit from the presence of an SPO and so it is difficult for SPOs to further expand their membership. To successfully strengthen and grow their businesses, SPOs need to develop processes to become more efficient at managing their members. One challenge is to ensure that all members have the necessary commitment and capacity to supply quality beans and are able to maintain organic and Fairtrade production standards. Failure to monitor a large membership base creates the risk that an SPO could lose its certification, and with it, its buyers. When monitoring members, SPO-4 categorizes its members as red (high risk of non-compliance), yellow (attention necessary) and green (reliable producers who need little attention). SPO-4 says that farmers in the area: "sometimes have the attitude that they know how to grow coffee because they have for generations." However, if they are not willing to change their practices in terms of plastic waste management, logging, hunting and farming steep slopes, then the SPO will suspend their membership. Dozens of non-complying members are removed from SPO-4's books each year.

5.6 CAPABILITY TO DELIVER ON DEVELOPMENT OBJECTIVES

Both men and women farmers expressed satisfaction with the services provided by their SPOs. Farmer views on the type and quality of services provided by the SPO were similar to those of the SPO leaders. Some specific topics are mentioned below in relation to production and marketing.

5.6.1 Production

SPOs deliver regular training for farmer members via paid staff as part of the ICS. Their main function is outreach and support to farmer members to ensure that they are complying with both organic and Fairtrade certification rules and regulations. During FGDs, members reported being satisfied with these services when they focus on good agricultural practices (GAP) to boost production. Some SPOs recalled how farmers can initially be reluctant to abide by environmental rules, such as planting on steep slopes, when they feel it is a constraint to production. However, in FGDs, all members said that they have come to understand

the purpose and importance of these regulations. SPOs perform regular checks on members, and if they are unwilling or unable to meet the requirements of the ICS, their group membership is suspended so as not to risk the certification status of the SPO.

5.6.2 Marketing

The main service that SPOs provide to members is a strong marketing outlet. SPOs typically work with traders and exporters to identify buyers, negotiate favourable prices, liaise with exporters on terms and sign contracts. Most SPOs were formed with the intention of gaining power in the marketplace and realizing higher prices and improved market access. All SPOs have much more power to negotiate favourable terms than individual farmers had at the end of the civil war only ten years ago.

SPOs also undertake processing to varying degrees. Business-led SPOs are often connected with sister processing and trading companies to such an extent that they appear integrated. These sister companies are often owned by members of the SPO's executive board. Business-led SPOs tend to have highly sophisticated operations, and can process from cherry to parchment (gaba), to wet asalan (labu), and green asalan (hulled, dried, and ready to export).

Farmer-led SPOs tend to be less sophisticated and own much less equipment, land and facilities. Warehouses and office spaces are typically rented rather than owned by the SPO. Processing coffee to export-quality green asalan is usually carried out by a third party (generally the export trading company), due to a lack of SPO facilities and staff capacity.

Most SPOs sell less than 50 percent of their production as Fairtrade, with the remainder sold on the local market. In practice, selling on the local market often means supplying the same exporters and middlemen, just without a Fairtrade contract. All SPOs would ideally like to sell all of their coffee on Fairtrade terms but this is only possible if there are enough buyers. That remains an ongoing challenge.

6. Experience with the Fairtrade Standards

6.1 CERTIFICATION PROCESS

Business-led cooperatives were the first to learn about Fairtrade certification around 2010, due to their close connection with buyers who informed them of the concept. In many cases, the exporter/trading company most closely associated with the cooperative applied for and paid for Fairtrade certification. Farmer-led cooperatives applied for Fairtrade certification a few years later.

SPOs cited three main factors why the certification process with Fairtrade was difficult:

- Firstly, information on the Fairtrade Standard is not available in Bahasa, and very few people in the area speak English.
- Secondly, at the time when most SPOs were seeking certification, the Fairtrade International associate staff member was based in Jakarta, which SPOs said resulted in limited contact and support.
- Thirdly, SPOs were often unwilling to help other SPOs navigate the Fairtrade certification process, partly because they viewed each other as competition.

All SPOs said that they initially lacked basic knowledge of Fairtrade processes and requirements, and all reported that they lacked sufficient information and support from Fairtrade when applying for certification and complying with the Fairtrade Standards in the first few years. SPOs said they had little idea of who to talk to during the application processes and did not have good contact with Fairtrade associate staff. This is partly because the Fairtrade office was based in Jakarta. In 2016, a new Fairtrade staff member based in Sumatra was recruited, which should address the issue of low contact with SPOs. The lack of access to fast and reliable information on Fairtrade processes was an initial constraint faced by SPOs. At the time of the research, some of the smaller SPOs still perceived this to be a limitation.

SPO-6 recalled how most other SPOs were not forthcoming with information on how to apply successfully for Fairtrade certification, due to the fact they considered them competitors. Fortunately, an existing business relationship between one of the executive board members and another SPO

leader helped them to access the information they needed and learn from their experiences. The SPO that assisted them provided template examples and helped them through the process. SPO-6 said this greatly helped them, particularly in addressing any non-conformity issues.

Like many other SPOs, SPO-7 had difficulties with the English language in Fairtrade documents. They reported approaching other SPOs, who were generally unwilling to help. However, a farmer member who had recently left another SPO was extremely knowledgeable and provided necessary insight. SPO-7 also recalled that around 2010, one woman at Fairtrade spoke Bahasa and was very helpful. SPO-7 said they heard that the Fairtrade Standard has now been translated. However, this is yet to be verified, does not appear to be online, and no other SPOs knew of this.

Two SPOs resorted to paying university students to translate some of the Fairtrade documents into Bahasa, but these were not shared with other SPOs. One SPO said that this translation cost US\$1,500 (€1,400). Other SPOs said they relied on Google Translate, which SPOs generally believe “gets the main points across.” The researchers viewed a summary of the Fairtrade Standards, translated using Google Translate, which was printed as a poster on the wall of one of the SPOs. A related limitation was poor internet and mobile network access by SPOs in rural and mountainous areas. However, this situation is improving. To help avoid misunderstandings, it would be ideal if Fairtrade translated its main documents into local languages where there is clear demand for them.

As discussed earlier, most SPOs were encouraged to become Fairtrade certified by traders and exporters. Later, when other farmer groups saw the benefits of Fairtrade certification they took it upon themselves to explore the possibility of Fairtrade certification. SPO-5 appears to be an exception, in that they were approached by Fairtrade who suggested they become Fairtrade certified. When SPO-5 applied, they did not have the correct internal procedures, such as a delegate system, regular village level meetings, or a Premium plan or training plan. SPO-5 said they were: “shocked because they had never seen anything like this before and felt unprepared.” However, Fairtrade helped them to understand the requirements sufficiently. While the account of SPO-5 is positive, all other SPOs said that Fairtrade

was in the field more frequently around 2010 than they are now, and they worry for new SPOs trying to go through the certification process.

Farmer-led SPOs also faced challenges in raising capital to pay for Fairtrade certification. SPO-7 recalled how, in addition to paying application fees for certification, the SPO also had to cover the costs of village meetings (food and fuel) for sensitization. The SPO took out a loan from the relatives of board members for the application process and basic office establishment. Taking loans out for Fairtrade certification was also a risk for the SPO and its board members. SPO-7 members were not initially convinced about Fairtrade certification due to environmental requirements, particularly restrictions on cutting trees, planting on slopes, and the establishment of buffer zones for water protection. Essentially, they were concerned about the extra labour involved, and that they would be constrained from expanding their farms in future. This required a lot of sensitization, promises of higher prices, and the SPO providing avocado seedlings to plant on slope areas.

Some of the first SPOs in the area have been Fairtrade certified for six years, and Fairtrade has higher requirements for SPOs certified for this length of time. These established SPOs expressed some frustration that Fairtrade does not sufficiently take into account the difficulty in maintaining quality from thousands of members, or the training of new members each year (dropouts and recruitments occur annually). Furthermore, these SPOs say that some of the technical aspects such as energy saving and renewable energy are new issues that they have no knowledge of. They say that waste handling is the most difficult because they are not allowed to burn or bury waste, and do not know who to consult to know what to do with the waste instead. SPOs say they have tried to discuss this with FLOCERT's Indian auditors, who replied that SPOs should take up issues with the local Fairtrade office. The SPOs say they have tried to do so but have not received assistance in this regard.

6.2 AUDITING PROCESS

SPOs consider the Fairtrade certification and auditing process to be rigorous, but understand that Fairtrade rules exist to ensure good governance. Farmer-led SPOs said they thought that they were ready to meet the requirements when they applied, but in hindsight they realized they "had little idea what they were getting themselves into." One SPO said that initially they "did not know how serious the Fairtrade auditing process was, because [they] had

not experienced anything like this before, including with organic certification." Several SPOs discussed how negative initial experiences with the auditing and certification process discouraged them. Nevertheless, when corrective measures were well explained to SPOs, they took note and did what was in their power to change. Many SPOs remarked how the Fairtrade rules and regulations have "opened their eyes to reflect," and have "helped them to slowly understand how these things are important for good governance." SPOs discussed how their executives, delegates and members have learned about transparency and proper governance structures as a result of the auditing process.

SPOs frequently expressed dissatisfaction with the Fairtrade communication channels saying they were unable to access support on rules and audit-related issues. When misunderstandings occurred, they would have benefitted from being able to ask questions and receive prompt responses. For example, since FLOCERT stopped using European auditors and began using Indian auditors, SPOs have observed a lower and slower responsiveness in communications; different interpretations of the rules; and some intercultural communication issues. All interviewed SPOs said that they preferred the European auditors because "they knew the context, whereas the new auditors do not seem to know much about the coffee business." SPO-6 remarked that "European gaps are only in language, but they otherwise understand us well." Some SPOs also noted that "there are also historical differences with Indians, and this is felt also."

SPOs said that they did not know why the change to Indian auditors was made, and they should have had a say on it. SPOs say that this has been brought up at national and Asia Pacific meetings, but SPOs suspect that the messages discussed in Asia Pacific meetings do not go any further and perceive India as having a dominant and controlling position in the meetings. It is possible that messages were communicated by FLOCERT, but if so, they do not seem to be reaching Indonesian SPOs.

Several SPOs also expressed concerns about delays in their communications with FLOCERT, the certification body which conducts audits for Fairtrade. For example, SPO-5 said that they have not been receiving proper notifications regarding audits. On one occasion they did not receive their audit information pack, and when they followed up and wrote to FLOCERT, they did not receive a response or an audit that year. This concerns the SPO, because they do not want a misunderstanding to lead to a suspension.

SPOs are naturally concerned when the Fairtrade audit does not go smoothly because they feel that the future of the SPO is dependent on retaining Fairtrade certification. They therefore take Fairtrade rules very seriously, and most SPOs expressed a fear of non-compliance and suspensions because they had seen other SPOs fail audits and then be disbanded. Therefore, it is understandable that delays and a lack of good communication cause SPOs much stress. SPO leadership appeared to genuinely view audits as a way to benchmark their progress and demonstrate to their members that the SPO is well run.

Several SPOs complained about the length of time it takes for an audit report to be drafted and for the results to be received, stating that European auditors used to send the report much quicker, giving them the maximum time to address non-conformities. SPO-5 said that since their last audit, six months have passed without receiving feedback on changes to be made. In recent years, they say they have had to wait up to 11 months for this information. The SPO says that they support the audit process and they need this feedback for their own organizational learning and to prepare for the next audit. The SPO would also like to receive copies of the full audit report, and do not understand why they only receive a summary sheet. The SPO has written several emails to the FLOCERT officer (filed and viewed by the researcher), but these have gone unanswered. SPO-8 is also concerned as they have not had an audit for two years, despite receiving and paying an invoice, and their queries have not been responded to. SPOs must learn to keep a paper trail of all actions and events so they have recourse if things go wrong. Many SPOs are weak at logging communications on important matters.

SPOs were asked why they do not direct their questions to the Association for Fairtrade Indonesia (AFI). SPO-8 says this is because AFI board members are also operating on the executive boards of other competing SPOs and do not want to share commercially sensitive information. SPO-8 says that they are not aware of clear guidance as to which issues should be communicated with whom, be it AFI, FLOCERT or the Fairtrade representative. This guidance may exist but there appears to be a lack of awareness among SPOs around the proper communication channels for certain issues.

Auditing can negatively affect an SPO if processes are not well understood. SPO-7 recalled how one Indian auditor was very strict, “unwilling to listen and had questionable ethics.” The auditor arrived on a day when a member had a death in the family and other members were grieving at the house. The auditor insisted on interviewing the member and did not respect local customs such as removing shoes before entering the house. He also insisted on entering the house unannounced to check certificates – including during prayer times – with the suspicion that members were hiding something. The auditor asked for land title certificates, which members were not willing to show as they believed this was not a requirement of the audit, and because they suspected the auditor wanted to “steal their land”. The auditor also allegedly refused to hold group meetings due to the smell of tobacco from farmers’ cigarettes. The SPO leaders recalled how farmer members were so angry they turned up at the SPO offices armed with knives and had to be reasoned with. Members said they appreciate Fairtrade, but expressed to the SPO that if such an event happened again they would refuse the audits and withdraw from Fairtrade.

SPO-7 had further difficulties when they were temporarily suspended following the audit. The SPO mistakenly thought that this meant that they could not fulfil a large contract that was already signed for. This misunderstanding nearly lost the SPO their exporter and buyer. The SPO appears to have misinterpreted the Fairtrade Standard due to the language barrier, which highlights the importance of the Standard being available in the local language⁶, and the importance of prompt communications with Fairtrade and FLOCERT when issues arise.

Passions surround the auditing process. If audits are not sensitively conducted, the process can lead to discord between farmer members and SPO leaders, negatively affecting the strength of an SPO. Fairtrade should be aware that auditors wield considerable power, and that their judgements can have a major effect on the SPO’s business relationships, its members, and ultimately, SPO strength and sustainability. Examples such as SPO-7 illustrate the weak position of SPOs to challenge auditor decisions. The change to Indian auditors has troubled some of the Indonesian SPOs, and

6 From the Fairtrade Standard 2.3.1: You do not sign new Fairtrade contracts if: i) your buyer is suspended; or ii) you are suspended; unless you can prove that you have existing trade relationships. If you do have existing trade relationships you can sign new contracts with this partner but the volume is restricted to up to a maximum of 50 percent of the volume traded with each partner in the previous year. In all cases you must fulfil existing Fairtrade contracts during the suspension period. Guidance: The contracts can be cancelled only if you and your buyer both agree to it in writing. The certification body will determine whether an existing trading relationship exists.

perhaps Fairtrade should look at whether further intercultural communication training is necessary.

6.3 TEMPLATES FOR REPORTING

Fairtrade could help to strengthen farmer-led SPOs through the provision of reporting and financial management tools, and basic training on how to use these. Some SPOs said that the Fairtrade reporting outline for annual reports has been helpful. In addition, SPOs would like a reporting format for their Fairtrade Premium plan and for financial reporting. Tools for reporting,

planning and financial management are especially important to help professionalize farmer-led SPOs, because most staff do not have business training, a university degree, or prior experience managing a business.

6.4 NEW STANDARDS FRAMEWORK (NSF)

SPOs in the research sample did not have any knowledge of the NSF. A possible reason for this is that most SPOs were Fairtrade certified after 2010, around the time that the NSF was established.

7. Conclusions

7.1 SERVICES TO MEMBERS

Both men and women farmers expressed satisfaction with the services provided by their SPOs, and member views closely aligned to those of their SPO leaders. In terms of production services, members are generally satisfied with the level of training provided on GAP and Fairtrade Standard requirements. While members initially expressed some reservation about modifying their production practices for Fairtrade, there is now broad agreement that Fairtrade rules and regulations promote positive changes in member villages.

Marketing services are the main reason why members join an SPO. Many SPOs formed with the express aim of improving the position of smallholder coffee farmers in the value chain. SPOs have clearly been able to secure more power to negotiate prices and dictate terms than individual farmers. Business-led SPOs have a particularly good command of the value chain and, in some cases, can perform processing up to export quality. Farmer-led SPOs have less capacity to process and are much more dependent on trade and export partners, however most have still made good progress since their formation less than a decade ago. SPOs and their members are particularly attracted to Fairtrade contracts because of the opportunity to receive a Premium. However, SPOs continue to have difficulties finding Fairtrade buyers, and typically less than 50 percent of their estimated production is sold as Fairtrade certified.

7.2 GOVERNANCE AND MANAGEMENT

SPOs were found to have good governance processes, as per the Fairtrade Standard requirements. Elections are held every three years for SPO leaders and delegates, and these are widely perceived to be transparent and democratic. Nevertheless, SPO executive boards are rarely voted out for a variety of reasons. SPO leaders often have a high status in their communities, are well connected in the coffee industry, have considerable experience and networks, and may be the owners of the trade and export companies that partner with the SPO. Therefore, electing new board members can risk disrupting the functioning of the SPO.

Members clearly feel they have a voice in the SPO and can freely express their concerns via their delegates. SPO leaders and members were overwhelmingly positive about the delegate system, which was not in place prior to Fairtrade certification. Nevertheless, members expressed little interest in the day to day management of the SPO, and are mainly interested in selling as much Fairtrade coffee as possible in order to generate Premium funds.

Members are positive about the process of choosing how Premium money is used. Delegates are presented with the financial position of the SPO annually at the AGM. Members vote via their delegates on how the Fairtrade Premium should be invested. The Fairtrade Premium is a major factor in SPO strength because it generates the working capital for SPOs to deliver services to their members, which in turn, helps SPOs maintain

members. Large business-led SPOs are also able to generate margins from coffee sales, however smaller farmer-led SPOs struggle to do the same due to the higher costs involved in outsourcing coffee processing. Few SPOs are looking to expand their membership further and most are trying to consolidate their market position and membership. SPOs indicated that there are now very few villages where coffee farmers do not already have access to an SPO.

7.3 SUSTAINABILITY AND RESILIENCE

Business-led SPOs are stronger than farmer-led SPOs, and face different prospects with regard to sustainability and resilience. Business-led SPOs have a strong presence in the sector and are fully integrated in the value chain, performing all processing stages up to export. Farmer-led SPOs are more vulnerable to various shocks. The strength and sustainability of farmer-led SPOs is largely dependent on their relationship with processing and trading companies, which link the SPOs to buyers. Furthermore, the organic certification of farmer members is often held by a trading company, and not by the SPO itself. Therefore, smaller farmer-led SPOs are vulnerable if the business relationship with their partner breaks down.

The resilience of several farmer-led SPOs has been tested in recent years due to price shocks. SPOs that signed contracts with long-term delivery dates encountered major issues when local and international prices spiked six months later. Some SPOs were unable to buy their members' coffee at a price close to the local market price, and faced either incurring large losses or defaulting on contracts. This had a considerable impact on several SPOs, and their ability to survive was partly down to whether or not the buyer was willing to renegotiate the contract. During this period, SPOs appear to have lacked access to reliable support and legal advice. However, it appears that all interviewed SPOs have learned their lesson and no longer sign contracts with fixed prices or delivery periods of longer than one month.

Some shocks have been unforeseeable such as a large earthquake in 2013, which severely damaged several SPOs and member villages. The Fairtrade Premium was extremely important for SPOs enabling them to respond to the emergency and provide support to SPO members at the time. Other shocks are predictable, with several farmer-led SPOs having been afflicted by computer viruses and hardware failures, which have led to the loss

of important documents. Most SPOs do not have basic digital backup processes.

7.4 BUSINESS PRACTICES

Business-led SPOs have strong systems and manage their operations as an established business. Farmer-led SPOs however, have much weaker systems in place, less experienced staff, and are constrained from making necessary improvements by a lack of capital. SPOs consult with their members via delegates when considering a new contract. While in theory this means that members are committed to fulfilling a contract, in practice, members still expect to be paid close to the local market price or higher. SPOs must be strategic and assess the market well, and be prepared to turn down contracts that are too risky. One SPO described the market as "full of tactic." Business practices in the sector are not always ethical, and several SPOs have found themselves in situations that threaten their sustainability.

7.5 EXTERNAL RELATIONS AND PARTNERSHIPS

The success of an SPO is closely linked to the support it receives from its trading and export partners. Trading companies and exporters have been vital to the growth of most cooperatives, because they link SPOs to buyers and export markets, pay for organic and Fairtrade certification on behalf of the SPO, engage in coffee processing, and often provide advance payment to SPOs to buy coffee from their farmer members. Most SPOs have only one trading partner, who strongly encourages the SPO to trade solely through them. Larger business-led SPOs have particularly strong external relations because the export and trading partners are often owned by members of the SPO executive board. In two cases, large business-led SPOs are able to manage the entire value chain and export process themselves. Most SPOs have difficulties finding new Fairtrade buyers, and few sell more than 50 percent of their estimated production as Fairtrade. All SPOs would be interested in increasing the share of members' coffee sold as Fairtrade, primarily because of the attractiveness of the Fairtrade Premium.

7.6 EXPERIENCE WITH THE FAIRTRADE STANDARDS

Most SPOs had difficulties when first working towards the Fairtrade Standard. Firstly, information on the Fairtrade Standard is not available in Bahasa, and very few people in the area speak English.

Secondly, at the time most SPOs sought certification the Fairtrade office was based in Jakarta, which SPOs said restricted contact and support. Thirdly, SPOs were often unwilling to help other SPOs navigate the Fairtrade certification process, partly because they view each other as competition.

SPOs consider the Fairtrade certification and auditing process to be rigorous, but understand that the Fairtrade rules exist to ensure good governance. However, when misunderstandings occur, they wish to be able to ask questions and receive prompt responses. Communications with FLOCERT and Fairtrade Indonesia are not as

smooth as SPOs would like. Several SPOs expressed concerns about the change from European auditors to Indian auditors, including the responsiveness of auditors, occasional missed audits, and cultural sensitivities. The SPOs take the audit process extremely seriously, because they have seen other SPOs decertified and understand that the strength of the SPO is linked to Fairtrade certification and receiving the Fairtrade Premium. The Fairtrade Premium is the biggest source of revenue for most SPOs, enabling them to invest in improved services for their members, and to strengthen the SPO position in the chain.

8. Recommendations on how Fairtrade can help SPOs become stronger

Based on the findings of the study in Indonesia, we recommend the following areas where Fairtrade can better support the strengthening of SPOs.

reviewing failed SPOs as a way to understand why they could not sustain their business or adhere to the Fairtrade Standards.

8.1 LINK SPOs TO POTENTIAL BUYERS

SPOs require much more support to identify new international buyers. Most SPOs sell less than 50 percent of their estimated production as Fairtrade, and would like to increase the volume of Fairtrade coffee sold. Examples of support could include international trade fairs, a directory of SPOs on the Fairtrade International website, or support to establish a separate website with details of SPOs producing Gayo Sumatra coffee.

8.4 IDENTIFY RELIABLE LEGAL SERVICES

On occasion, SPOs require access to legal representation. However, SPOs lack confidence in legal services to be reliable and fair. Fairtrade could work with SPOs to identify reputable legal service providers who are knowledgeable about the coffee sector.

8.2 OFFER BUSINESS DEVELOPMENT SUPPORT

Farmer-led SPOs would benefit from further business development training and support. While business-led SPOs are led by experienced business people, farmer-led SPOs often lack the same capacity to run the SPO as a business. Fairtrade should consider the resources it has available to help farmer-led SPOs better manage risks, identify new opportunities, and manage the SPO as a business. This requires more than a one-day training activity.

8.5 TRANSLATION OF FAIRTRADE DOCUMENTATION INTO LOCAL LANGUAGE, I.E., BAHASA

The Fairtrade Standards and procedures would be easier to follow if translated into Bahasa. SPOs have encountered much difficulty with Fairtrade documentation because few people speak English in the area.

8.3 REVIEW FAILED SPOs

SPOs suggested that there are lessons to be learned from failed SPOs. Fairtrade could consider

8.6 IMPROVE AVAILABILITY OF THE FAIRTRADE ASSOCIATE STAFF

SPOs have found it difficult to contact the Fairtrade representative living in Jakarta. The organization has since hired an associate in 2016 who lives in Sumatra, which should greatly improve communications between SPOs and Fairtrade.

8.7 IMPROVE COMMUNICATION AND RESPONSIVENESS ON AUDIT-RELATED ISSUES

The Fairtrade auditing process is a serious issue of concern for SPOs and there is discontent about the change from European to Indian auditors. Fairtrade and FLOCERT should review where improvements can be made in terms of responsiveness to SPO feedback and questions.

KIT Royal Tropical Institute

Mauritskade 64
1092 AD Amsterdam
The Netherlands

Phone: +31 (0)20 568 87 11
For enquires: m.tyszler@kit.nl
Web: <https://www.kit.nl/>



KIT Royal
Tropical
Institute