



The role of voluntary sustainability standards in scaling up sustainability in smallholder-dominated agricultural sectors

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This research forms part of a project funded by the International Finance Corporation, the Dutch Ministry of Foreign Affairs, SECO and IDH the sustainable trade initiative in which Aidenvironment, NewForesight and IIED sought to develop a holistic transformation model to scale sustainability in smallholder dominated agricultural commodity sectors.

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Introduction

Concerns about the sustainability of commodity production have increased rapidly in the last decade, resulting in a call for consumer and supply chain responsibility. Failing public sectors paved the way for the emergence of market-driven initiatives, notably voluntary sustainability standards (VSS). VSS have become a dominant instrument to promote sustainability in many commodity supply chains. As the reach and impact of VSS become more visible, we are reminded that VSS are not the solution for every sustainability challenge. Indeed, this was never their intention. While VSS try to respond to a call for increased scale and impact – at low cost – creating fully sustainable sectors demands complementary or alternative approaches. This is especially necessary in sectors dominated by unorganised smallholders where increased capacity building, input delivery and finance, as well as other systemic changes such as land tenure, are prerequisites for a viable and sustainable sector. Mainstreaming sustainability in such sectors requires a more holistic model that achieves scale beyond individual supply chains.

This paper begins with an introduction to VSS' current value proposition, some of the challenges they are confronted with and how their typical response to these challenges. It then presents a more holistic model to scale sustainability in smallholder dominated agricultural sectors and explores the potential role VSS can play within such model.

Achieving sustainable markets through voluntary standards

VSS have been developed as a market-driven instrument for transforming sectors towards sustainability. The theory of change of VSS is that compliance with their standards mitigates negative social and environmental impacts and creates economic benefits. VSS have proliferated in recent years, with a scaling up of their adoption in several sectors. As of October 2014, the ITC Standards Map, a global database on VSS, had recorded more than 150 standards and codes addressing sustainability issues in global supply chains. VSS vary in nature (practice or performance based), scope (social, environmental, economic), ambition (minimum criteria versus best practice or fixed thresholds versus improvement approaches) and ownership (multi-stakeholder, NGO, non-competitive, private, public). Although there are many variations in the structure of VSS systems, their theory of change is based on a market demand driven value cycle (see figure 1) and a set of services (see figure 2) to achieve positive social, environmental and/or economic impacts.

Driven by demand for sustainable products, producers and/or manufacturers are required to implement a set of practices or obtain a certain level of performance. A VSS provides the normative description of the required practices or performance. A sustainability claim can be made where evidence of compliance with the VSS requirements is provided by a credible system of assurance. Evidence can be provided by self-verification (first-party), second-party verification (e.g., buyer) and independent, third-party verification (e.g., accredited certification body – certification

Figure 1: Standards value cycle

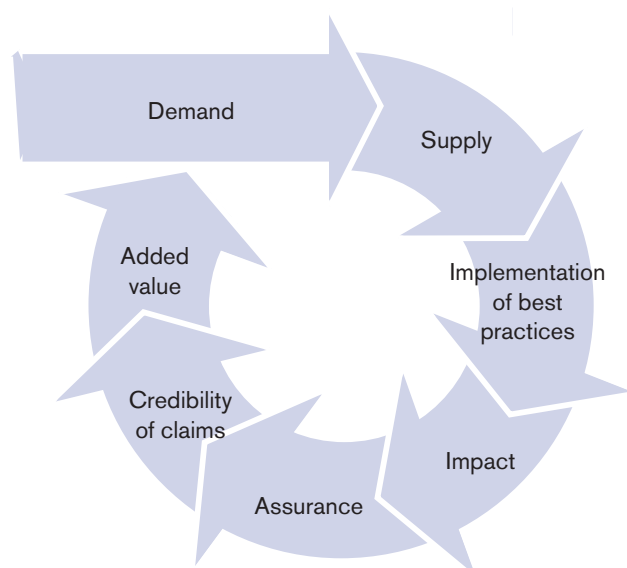
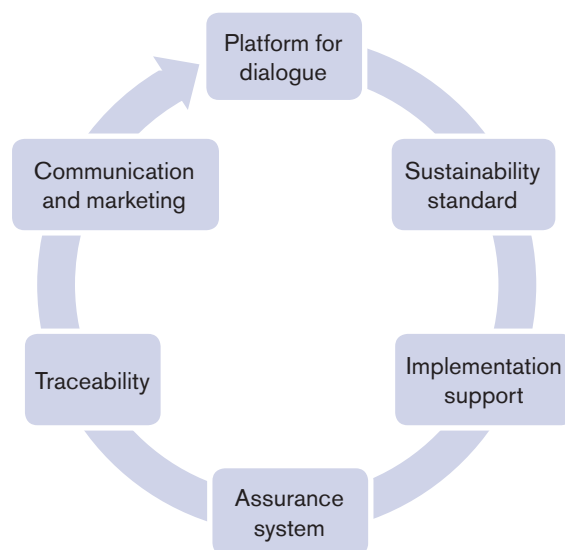


Figure 2: Core services of standards



being a formal judgement on compliance based on third-party auditors' reports). The credibility of the sustainability claim of VSS is stronger if its impacts can be systematically proven. The sustainability claim can be 'transported' along the supply chain, from producers to consumers and companies, by a chain of custody and traceability mechanism. The assumption is that the sustainability claim adds value for consumers and businesses, possibly by the use of a logo, and can thereby create market demand. Increasing demand drives the value cycle of VSS and leads to an increasing supply of sustainable products. The vision of VSS systems is that over time the value cycle transforms markets to only demanding sustainability products. This would result in a situation where compliance with the VSS is a licence to operate and pre-condition for market access (Aidenvironment & Jinke Van Dam Consultancy, 2013) and where production throughout a sector is sustainable. To accelerate the value cycle, VSS may provide support (e.g., training) to producers, create incentive mechanisms (e.g. premiums), and raise consumer awareness. Some VSS systems also add value by offering a platform for dialogue (e.g. roundtables) which can contribute to the creation of trust, alignment in vision and collective action.

VSS have been important instruments in promoting sustainability in a wide range of sectors. They have proved to be instrumental in:

- Providing a common reference for sustainability by operationalising the concept of sustainability into concrete practices and norms
- Building consumer, industry and producer awareness of sustainability
- Providing a platform for sector dialogue and governance

- Mobilising market driven incentives for sustainability
- Mobilising investments in producer organisation and training
- Promoting transparency in supply chains combined with assurance and traceability to substantiate sustainability claims

Challenges for VSS in scaling up and proving impact

In 2013, the share of global production in some of the major commodities that complied with a VSS ranged between 2 per cent (soy) and 29 per cent (coffee). In some commodity sectors VSS have shown spectacular growth (e.g. cocoa), while others have stagnated (e.g. cotton). The number of sectors in which standards have been introduced is also still increasing rapidly. However, while supply expands, demand does not always follow; in the major commodities there appears to be a structural oversupply of certified production with an average market uptake of around 50 percent.

Despite the rapid growth in supply and demand in some sectors there are concerns that this growth will soon hit a ceiling. These concerns are based upon constraints in terms of demand for certified products, the proof of sustainability impacts of VSS and the

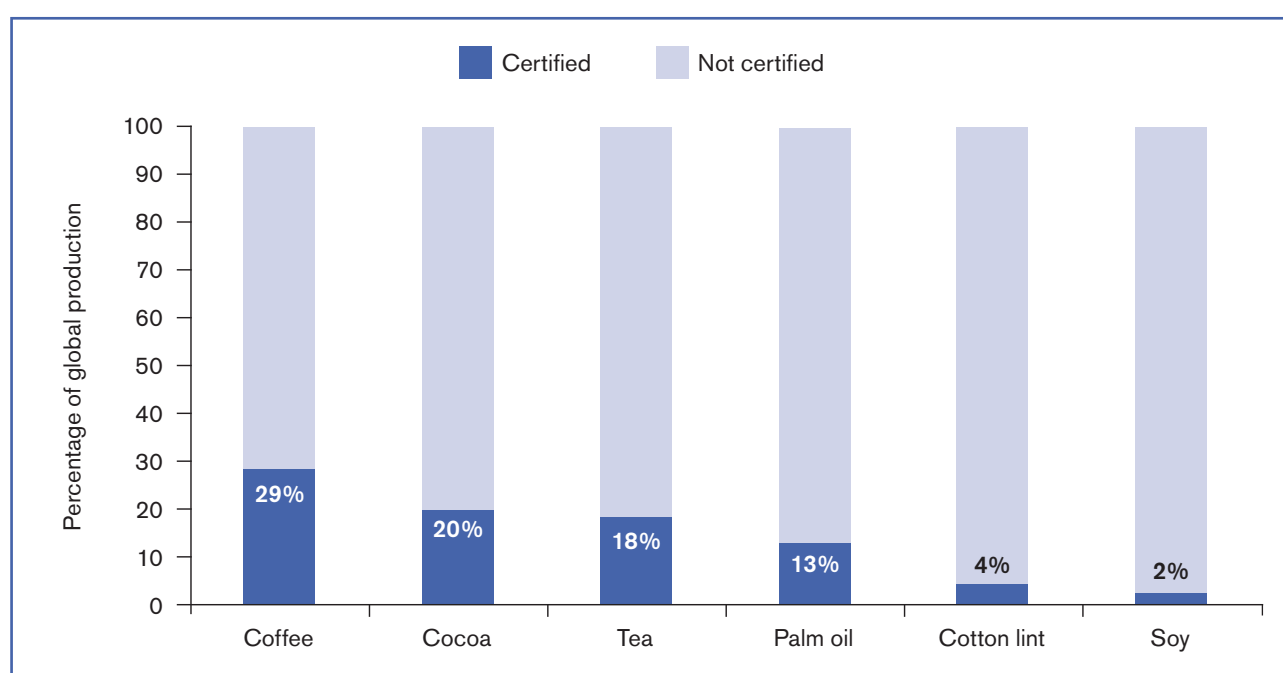
feasibility of scaling standards in sectors with a high proportion of smallholders, especially where they are not well organised.

Demand for certified production lags behind supply

A lack of demand compared to supply of certified produce is an issue of concern for a market driven instrument like VSS. This will only increase as the share in global consumption of many commodities shifts towards markets which have limited awareness of sustainability issues in commodity production and trade (e.g., emerging economies). In markets with higher levels of awareness, such as the USA and the EU, VSS are challenged to maintain and further increase demand. First mover companies often source certified or verified products to differentiate themselves from competitors; they believe it can protect the value of their brand and convince the consumer to buy their products. However, sustainability is still not a dominant driver of purchasing decisions for a large number of consumers.

In markets where VSS became successful, there is now a challenge to redefine their value proposition as their contribution to market differentiation of individual companies decreases. This challenge is increased by the emergence of public mandatory sustainability standards (e.g. EU RED or CEN/ISO), which are often less comprehensive in scope and less ambitious in

Figure 3: Certified (including verified) production (2013)



terms of sustainability threshold. These standards may dilute the sustainability claim of VSS in the marketplace and require additional efforts from VSS to prove their added value.

Increased demand for proof of impact and credibility

There is increasing concern about the impact of VSS. While the sustainability impacts most VSS pursue are comprehensive and ambitious, VSS have for a long time neglected to prove whether the implementation of a standard does result in the desired impacts, partially because they have been too busy promoting supply and demand for certified production. Investing millions of dollars in certification, the private sector, donors and consumers have started to demand accountability for their investments. As a result, VSS have recently invested more in performance and impact measurement. The results of these efforts to measure the impact of VSS are mixed. While in general the impact of VSS appears to be positive, they rarely contribute to a positive impact on all issues they aim to address. This lack of impact is partly caused by the fact that VSS focus on the farm level, while the root causes of the issues they need to address are often at community and landscape level and can be attributed to failures in policy and governance that VSS alone cannot address. In this respect, VSS may overestimate their potential impact and raise false expectations.

There are also limitations to verifying compliance with a standard. Some criteria, such as child labour, are difficult to control with a periodic audit. Persistent concerns over the quality and sometimes the integrity of auditors and concerns about double counting in multi-certified supply chains can further affect the credibility of VSS. These concerns about effectiveness and credibility negatively influence demand.

High costs and weak business case impede scaling up in sectors with unorganised smallholders

There is a concern about the complexity and costs of scaling VSS to producers who have not already been reached. In many sectors, there is a bias towards certification of the 'low-hanging fruit': the larger farmers or the better organised, accessible and capitalised smallholders that face fewer sustainability challenges. However, in many sectors most farmers are neither large nor organised, accessible or capitalised. Certifying the vast majority of small-scale farmers requires significantly larger investments

in organising and building capacity. It is doubtful whether market-driven mechanisms could raise these investments and consequently, a large part of the smallholder production base risks being excluded from sustainable markets.

VSS have been criticized for not prioritising productivity, quality and profitability. The economic viability of a farm and its contribution to a decent livelihood should be an integral part of what is considered sustainable. Productivity and quality are also important aspects in meeting the challenge of feeding 9 billion people in 2050 and reducing pressure on the land. Productivity, quality and profitability can be considered prerequisites for effective implementation of sustainability practices; through improved profitability, farmers have the greatest potential to pay for the social and environmental investments associated with VSS and certification. However, in many cases, intentionally or unintentionally, farmers have been attracted to certification by the promise of a price premium instead of a structural improvement in productivity, quality and profitability. In light of today's limited market demand this poses a number of risks in terms of the sustainability of the changes in farmer behavior: if farmers cannot sell their certified products with a premium, they may decide to drop out of the system. It is likely that as soon as they drop out of the system they revert to old practices. To date VSS, industry and other stakeholders, such as NGOs, have been unable to convince farmers of the intrinsic value of sustainable farming practices in the absence of a premium.

What is really needed in smallholder dominated sectors are investments that enable farmers to improve their performance structurally. Supporting farmers to improve their practices also requires large investments in capacity building. Most current VSS systems do not provide or promote enough of these investments; they only provide a reward after the investment has been made. The question that arises is whether a compliance based pass-fail approach is strong enough to incentivise and enable smallholders to change practices.

VSS are beginning to respond to challenges

The above challenges are not new and VSS are increasingly investing to address them. Recent innovations focus on increasing the accessibility of VSS to smallholders, reducing costs of certification, providing additional services and increasing demand in emerging and developing economies.

Shift from a single threshold pass–fail approach to step-wise or continuous improvement approaches

VSS are increasingly introducing standards that embrace step-wise and continuous improvement approaches. Some require a lower entry threshold and allow full compliance to be reached within a fixed (or flexible) timeframe. Others allow farmers a certain degree of freedom to define their own priorities with regards to the standard's requirements. Accessibility is also promoted by the development of national interpretations and smallholder interpretations as well as by enabling smallholders to become certified as groups.

Innovations in assurance approaches

The introduction of risk-based assurance models, possibly in combination with different forms of first- or second-party verification may reduce the frequency of third party audits and related costs. These new assurance approaches, such as self-assessment, peer reviews, or participatory assessments have the additional advantage of enhancing farmers' awareness and learning. There exists however a potential trade-off between less frequent and less impartial assurance approaches and the credibility of claims – especially if credibility is based upon ISO guidelines on assurance approaches.

The extent to which this trade-off is a problem partly depends on what one wants to prove and incentivise: the improvement process, or compliance with a certain threshold in order to determine whether someone passes or fails. If the first is favoured over the latter, than impartiality in assurance may become less important and more emphasis can be given to learning (Aidenvironment & Jinke Van Dam Consultancy (2013)). This requires a paradigm shift from proving compliance to enabling improvement.

Increased collaboration between VSS

Different VSS also aim to reduce the cost of implementing their standard by collaborating on certain issues. Some examples currently in place include:

- mutual recognition between VSS systems and harmonisation of certain requirements (e.g., living wage, list of prohibited pesticides)
- allowing joint audits, where compliance to different standards are assessed in one audit

- jointly developing training material
- promoting stepping-stone programmes between baseline standards and best practice standards.

Increased value to farmers and supply chain actors of VSS investments in complementary services

VSS increasingly deliver complementary services. These services include capacity building, credit or subsidy facilities, as well as farmer information services (such as weather forecasts). These services are delivered by the VSS systems themselves or in partnership with specialised service providers. They can be financed via the system (e.g. licence fees) and/or by external donors. Some VSS also increase their efforts to collect performance data at farm level which are valuable to the supply chain (e.g., yields, water footprints).

Promoting demand in emerging and developing economies

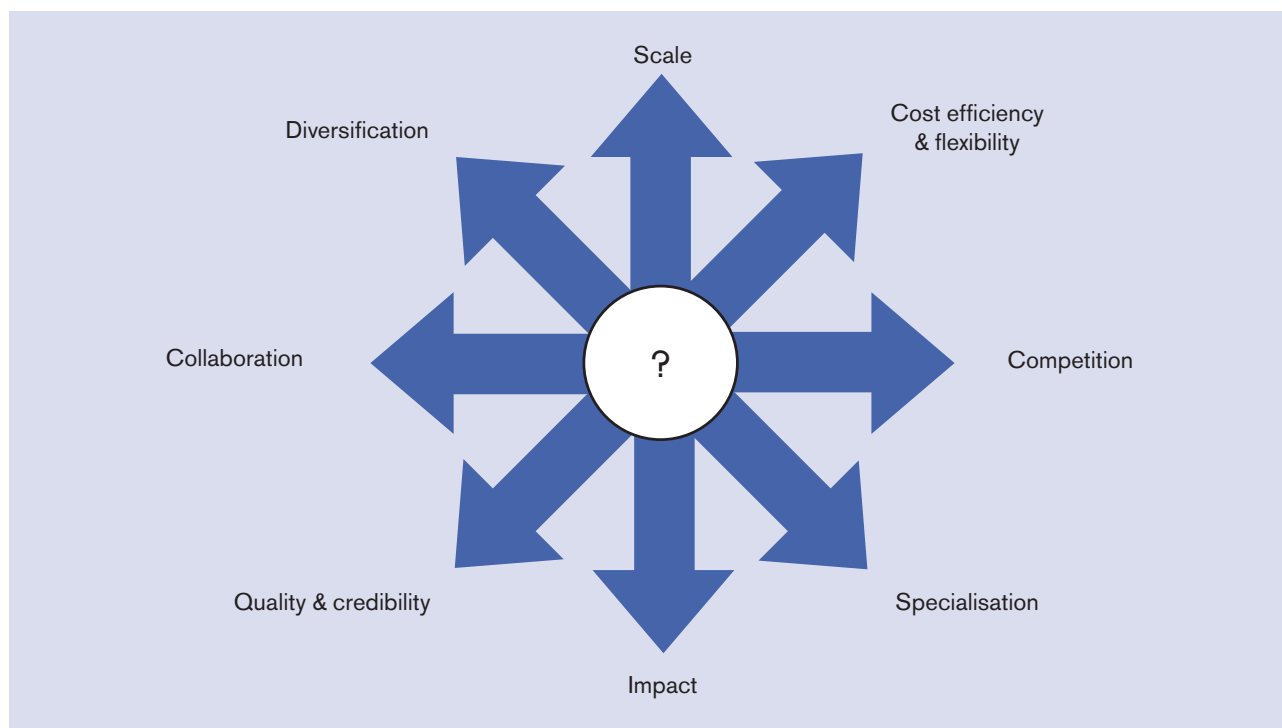
Some VSS increasingly invest in creating demand for certified products in emerging markets. They develop awareness campaigns or promote uptake via companies that operate globally.

Collaboration with the public sector to promote sustainability

A few VSS actively engage with the public sector in order to, for example, integrate the standard into public extension curricula or in national regulation.

Emergence of complementary and competing initiatives

VSS are not the only initiatives that innovate. Initiatives that either support or complement implementation of VSS, but also potentially replace certain services of VSS are increasingly emerging. The tools and initiatives that have been launched outside of VSS systems focus on monitoring, data management, developing feedback loops, step-wise improvement approaches, peer learning and capacity building. For example, some initiatives allow suppliers and farmers to monitor their performance, some include traceability modules, and others provide a participatory approach to guide improvement. Corporate programmes that build the

Figure 4: Dilemmas of VSS

capacity of farmers, address the root causes of priority issues and report on key performance indicators are also emerging.

While some of these emerging initiatives can be more efficient and effective than VSS in providing certain services, the question remains whether they can provide the scalable solutions that remove the fundamental barriers to mainstreaming sustainability in sectors dominated by unorganised smallholders.

The growing call for VSS to have impact at scale and at low cost, the emergence of alternative initiatives and intensifying competition between VSS puts them under significant pressure. VSS currently face dilemmas related to where to invest:

- Should they prioritise scaling up (in terms volumes or products) or focus on deepening impact?
- Should they compete or collaborate with other VSS and initiatives?
- Should they offer a complete system and diversify in new services or specialise in specific services?
- How should they balance the need for cost efficiency and flexibility with the need to deliver quality and maintain credibility?

It is not clear yet which paths the different VSS will choose.

Scaling up sustainability in smallholder-dominated sectors requires a more holistic approach that promotes farm and sector quality

The above dilemmas become more complex if one considers VSS as an instrument in isolation and as a dominant solution to sustainability challenges. Based upon the arguments above which include lack of demand, implementation costs, their potential impact, VSS should not be regarded as the only instrument to solve sustainability challenges. In the context of sectors dominated by unorganised smallholders – which is true of many agri-commodity sectors in developing countries – supply chain-based solutions such as VSS tend to create islands of sustainability, rather than creating the systemic changes that are needed to reach the majority of smallholders. To promote sector-wide improvement in sustainability performance, a more holistic approach is needed. Reaching out to different types of producer, requires different strategies. Supply chain-driven sustainability initiatives such as VSS may have a role, but to reach unorganised smallholders they need to be complemented or preceded by other approaches and investments. These investments should target both

the individual farmers as well as the sector as a whole. Improving farmers' income, yields and product value is a precondition for them to adopt comprehensive sustainable practices and thereby comply with social and environmental norms and regulations. To reach this goal, farmers must:

- be willing and able to invest in their farm
- have the capacity to use good agricultural practices and inputs
- be able to mitigate risks.

These requirements must be considered an integral part of sustainability performance at the farm level or what can be called 'farm quality'. Reaching this level of farm quality is only possible if certain conditions are achieved in the respective sectors. Sectors also have to perform on 'sector quality', by:

- ensuring access to high quality extension, inputs and financial services
- maintaining quality standards
- obtaining a certain degree of resilience of the overall sector in the face of market volatility and climate change.

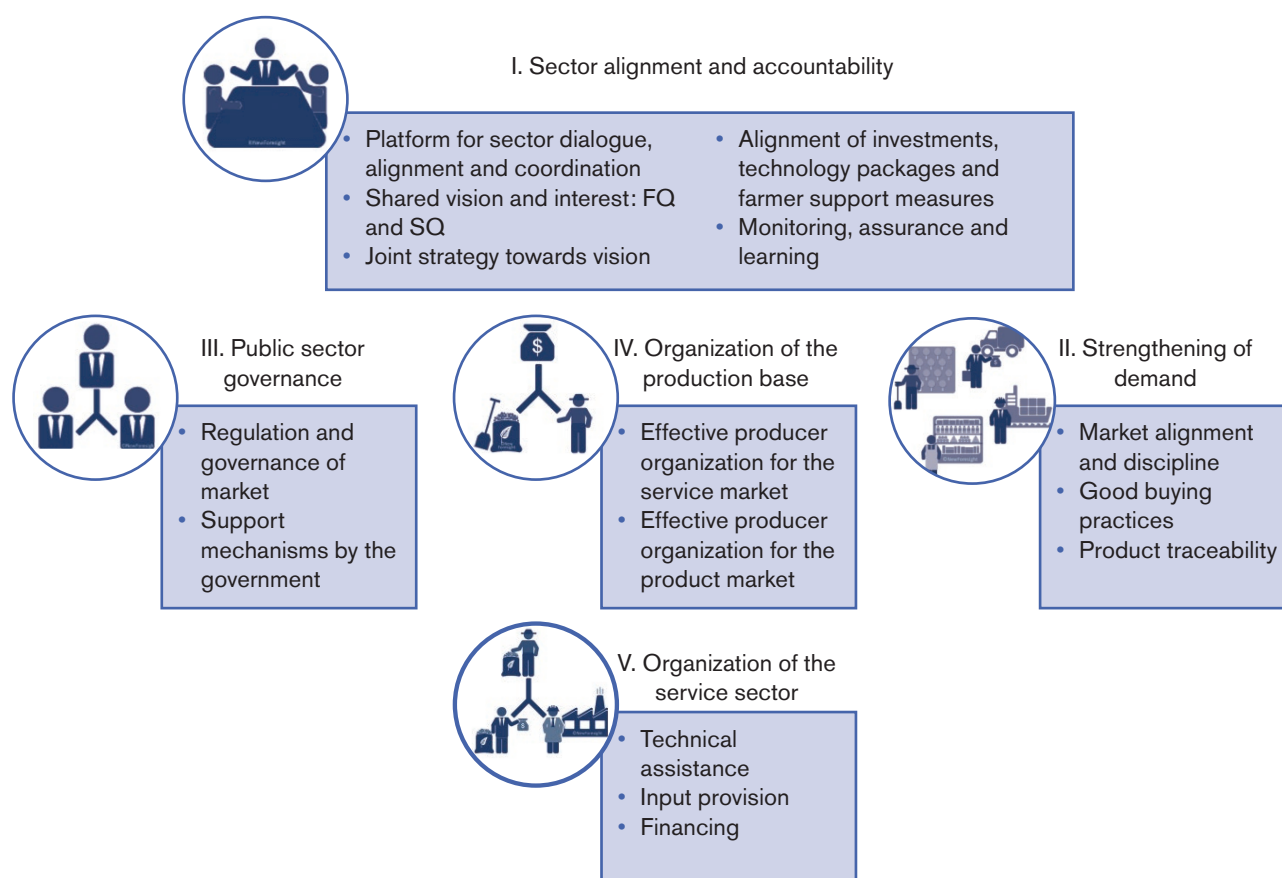
The sector also needs to differentiate and reward good performance on all aspects of farm quality and at the same time as removing worst practices from the sector.

They must also be able to capture a sufficient share of the value generated along the supply chain. This enables the sector as a whole to re-invest in sector quality, including aligning efforts to manage public goods and natural capital (at community, landscape or national level).

The promotion of both farm and sector quality requires a more holistic approach in which there are five key building blocks (see figure 5):

- *Sector alignment and accountability*: Crucial in this building block is the development of a vision on farm quality and sector quality, including the definition of a step-wise improvement path. This vision should be shared by all relevant stakeholders and translated into a strategy that clearly defines roles and responsibilities between stakeholders. Each stakeholder should be held accountable for key performance indicators (KPIs). Progress on the KPIs should be monitored and the monitoring data should be used to adopt the strategy and stimulate sector-wide learning.
- *Strengthening market demand*: The market should align behind the vision and organise their procurement practices in such way that it rewards improvement and excludes worst practices. This requires buyers to position themselves as preferred buyers to producers and possibly provide additional services such as capacity building or inputs.

Figure 5: The five building blocks for sustainable sector transformation



- *Public sector governance:* The public sector has an important role to regulate and support sector transformation where the market fails or is incapable of acting. This includes enforcing social and environmental regulation (for example, on land tenure, labour, and conservation), providing investments (e.g. infrastructure, research, input subsidies), and governing the market to ensure effective quality differentiation and price transmissions, reduce price volatility and improve sector organisation (e.g. minimum prices, quality regulation, marketing boards).
- *Organisation of the production base:* Key for wide-scale promotion of sector quality is to organise producers around service delivery. Organisation could be obtained in different ways, including through service provider networks, outgrower schemes, supply chain networks, cooperatives or sector-wide organisation. The organisation of the production base can enable the market to reward good performance and exclude worst practices.
- *Organisation of the service sector:* Services such as extension, inputs and finance need to be accessible, demand driven, bundled, where possible, and of high quality. In an ideal situation, services are provided by a competitive market of service providers that treat farmers as clients and in which services are increasingly paid for by farmers themselves. Service delivery should also reward good performance and exclude worst practices. In the absence of a professional service sector, buyers or the public sector could organise this alongside complementary, possibly non-competitive, investments to build a professional service sector. Small sector levies and taxes may offer potential for longer-term sector-wide financing of services.

The extent to which the above building blocks need to be strengthened is context specific, but a focus on only one or two dimensions is bound to lead to a failure to completely transform sectors where there are many unorganised smallholders.

VSS can play different roles in sector transformation

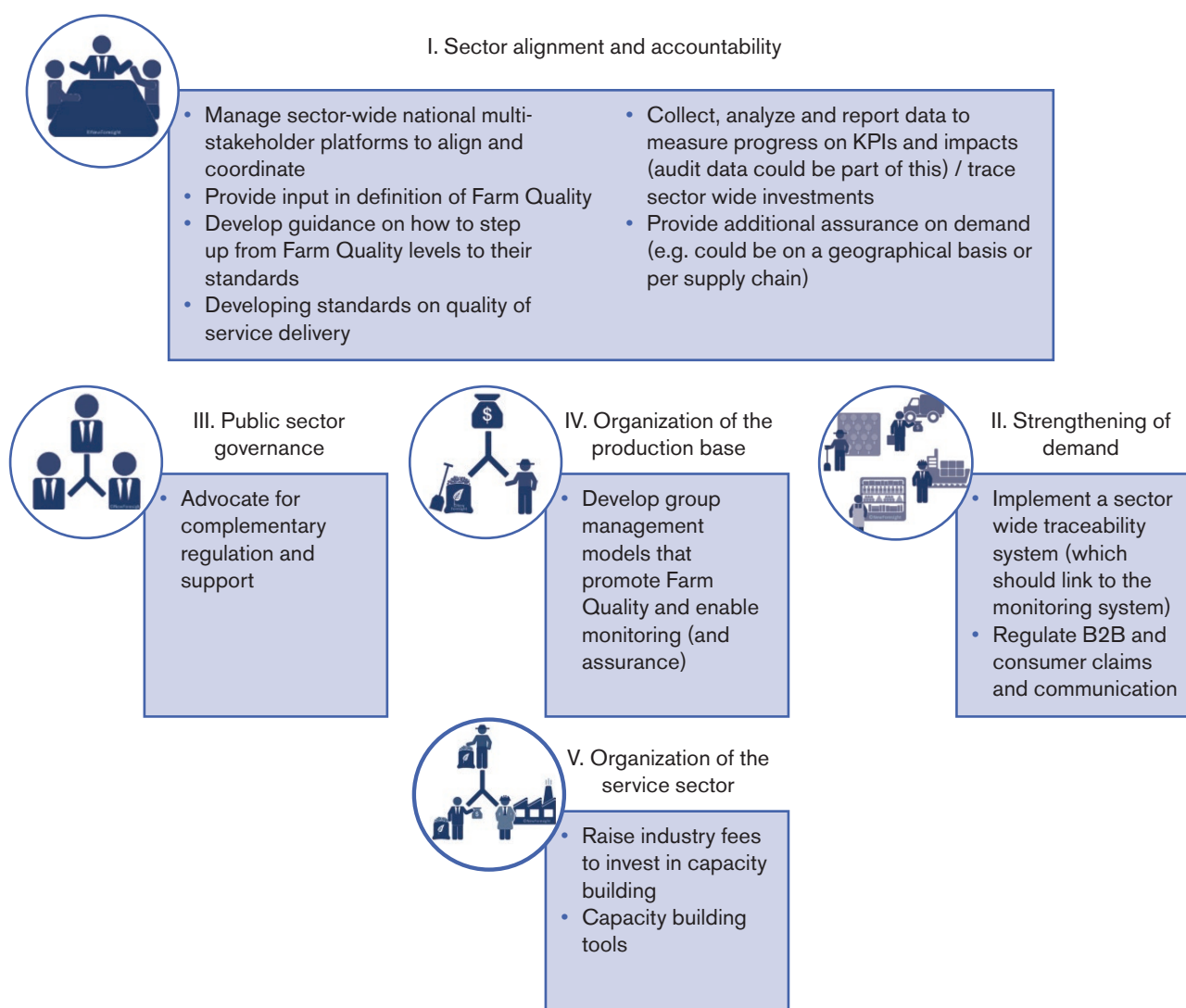
Within the sector transformation model presented above, VSS can play a number of important roles (see figure 6). Most likely, they can add value in the sector alignment and accountability building block, by, for example, managing multi-stakeholder platforms, similar to the roundtable concept, but at a national level. Creating links between national platforms and an international platform can be important to ensure global consistency. VSS can also provide input to the definition of farm quality and provide guidance in the

form of a step-wise approach in which the current VSS standards can be a point of reference. As capacity building is crucial in smallholder dominated sectors, it is important that the investments are of high quality. Developing quality standards for capacity building could be a service provided by VSS. VSS could also provide the tools to trace investments and collect data necessary to monitor progress and impacts, as well as to validate and improve the step-wise approach. Some VSS already invest in more sophisticated data collection and reporting systems. Redesigning these systems to a more geographically based system rather than purely supply chain-based measurement could be instrumental in achieving sector-wide transformation processes. As well as the monitoring activities, additional levels of assurance could be offered; these could be more participatory if the learning component is important or based upon third party audits if evidence of compliance is important.

On the demand side, VSS could continue providing traceability systems. While the need for full traceability may reduce if the monitoring system becomes stronger, linking traceability to monitoring can become an important feature in the intermediate phase. For those companies interested in having credible claims with regards to the sustainability of their supply, VSS can continue to provide labels and claims (business-to-business or consumer) based upon rigorous assurance. This could be combined with consumer awareness activities, although many other actors could also take up this role (including industry and NGOs).

Within the organisation of the production base organisational models that favour product markets or service delivery are required. VSS currently offer a group model built around an internal control system (ICS) which aims to enable certification and is predominantly centered on assurance. The challenge will be to offer the frameworks in which unorganised producers see the value in organisation in order to better access the services they need or better market the products they produce. These frameworks should emphasise principles such as continuous improvement, transparency, fair distribution of value, respect for rights, as well as collection and assurance. VSS can add value by offering the guidelines and mechanisms applicable to different types of organisation such as service provision networks, cooperatives, and supply chain-based networks.

With regard to the service provision building block, VSS could promote awareness-raising of farm quality, self-assessment, and peer learning tools for step-wise approaches to farm quality. Some VSS have already started to experiment with these kind of tools. Even more important, VSS could promote a reorientation of the financial resources currently raised in supply chains from paying cash premiums for capacity building. Incentivising investments directly appears to be more relevant in sectors dominated by smallholders

Figure 6: Potential roles of VSS for sector transformation

than offering a premium for the 'lucky few' who have been able to reach a given threshold. The current investments from the private sector in premiums could fund an important part of the capacity building needs in various sectors.

Finally, VSS can put more emphasis on collaborating with the public sector in order to tackle the systemic constraints that obstruct the improvement of farm and sector quality.

VSS at a crossroads: comprehensive systems or specialised complementary service provision?

A shift to a more holistic model of sector transformation will demand different roles or changes in the services VSS are used to providing. Instead of offering a

comprehensive set of standardised services (standard, assurance, traceability, etc.), they may need to adopt a modular strategy in which they offer specific high value services responding to context-specific needs. Acknowledging that VSS are part of a wider constellation of instruments opens up many more possibilities for complementary approaches and synergies between different actors, including industry, public sector, NGOs and the financial sector. While this may result in a different role for VSS than the one they play today, it could keep them in the forefront of enabling sustainable sector transformation.

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Aidenvironment and Jinke Van Dam Consultancy (2013), *Linking assurance, learning and impacts in voluntary standards systems*, commissioned by ISEAL Alliance.

This paper presents the value proposition of voluntary sustainability standards and the challenges they face in obtaining scale and impact in sectors dominated by unorganized smallholders. It explores their potential role in scaling sustainability within a more holistic sector transformation model.

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