



Agricultural cooperatives, responsible sourcing and risk-based due diligence

Executive Summary

Agricultural cooperatives are an integral part of the global agri-food system, providing essential jobs, income, and market access opportunities for smallholder farmers and others in agri-food supply chains in low- and middle-income countries. This policy brief introduces how agricultural cooperatives in developing countries can integrate risk-based due diligence into their business models to meet increasing market and legislative requirements related to sustainability and responsible business conduct in global value chains (GVCs). As downstream agri-food companies and traders begin to introduce sustainability requirements into their operations, their upstream partners and suppliers will also be required to demonstrate how they are managing social and environmental risks in their business operations. Agricultural cooperatives are essential actors to consider in these dynamics because many already participate in GVCs through commodity trade. Importantly, in developing countries, cooperatives are often at the heart of agricultural sourcing communities and can unlock significant opportunities for rural economic growth and poverty reduction. By adapting to changing market and legislative needs related to responsible sourcing and sustainability, cooperatives are better positioned to reduce adverse social or environmental impacts and improve their standing as a responsible supplier in GVCs.

Introduction

Agriculture is the leading source of employment and income in most developing economies. On a global level, the agricultural sector employs an estimated 1.3 billion workers, or half of the world's labour force (ILO, 2022). Moreover, approximately 80 percent of the world's extreme poor¹ live in rural areas, two-thirds of whom are employed in the agricultural sector (Castañeda *et al.*, 2018). As such, the agricultural sector is an enormous source of economic growth and development in low- and middle-income countries. However, business owners, smallholder farmers and producer organizations such as agricultural cooperatives often face structural barriers to access domestic, regional and global markets that can support trade and development. This includes challenges such as poor infrastructure, limited access to credit, and lack of technical knowledge and information on market standards, trade requirements, prices and technology. In addition to threatening their safety and health, these issues can affect productivity and negatively impact

development. Exploring ways to bolster sustainable and responsible business is important to lift poor agricultural communities out of cycles of poverty.

In developing and transitional economies, agricultural cooperatives are often in the front line of working with producers, including smallholder farmers. They offer a variety of extension services to their members, helping farmers boost yields and address food quality standards, among other benefits. In addition to building technical capacity, cooperatives also support development by ensuring that food security and nutrition receive due consideration in local communities. For several decades, cooperatives have played a critical role in the international development agenda, even celebrated in 2012 as the United Nations International Year of Cooperatives (United Nations, 2011). Yet, there remains a lack of research on how agricultural cooperatives feature in global supply chains. Cooperatives represent an important unit of analysis to understand how smallholders can better integrate into global value chains (GVCs), improve their

¹ Extreme poverty is defined as those living below USD 1.90 a day, as measured in 2011. See World Bank, 2021.

skills and support responsible business conduct (RBC)² in the agricultural sector.

The objective of this policy brief is to consider how cooperatives in global agricultural supply chains can be leveraged to reduce adverse environmental, social and development impacts in agricultural production and sourcing. This brief is designed to encourage dialogue on risk-based due diligence among agricultural cooperatives and enterprises by identifying ways to implement recommendations from the Organisation for Economic Co-operation and Development (OECD) and Food and Agriculture Organization of the United Nations (FAO) Guidance for Responsible Agricultural Supply Chains (OECD-FAO Guidance) and its five-step framework for risk-based due diligence.

Increasingly, many governments are introducing sustainability-related legislation that require companies under their jurisdiction to do more to limit adverse impacts in their supply chains, including through risk-based due diligence. While challenging, companies have the opportunity to encourage better development outcomes through responsible sourcing. From an enterprise and competitiveness perspective, this brief also introduces how cooperatives can adapt their activities and services to meet the changing market needs on sustainability, thus promoting themselves as responsible suppliers in GVCs. Finally, governments and other actors, such as non-governmental organizations (NGOs), may find this research useful in considering how agricultural trade and development policies can better support cooperatives in meeting downstream responsible sourcing requirements.

Risk-based due diligence and global agricultural supply chains

Many supermarkets in high-income countries import or source commodities and processed foods from low- and middle-income countries. For agricultural producers in these countries, increased international trade can deliver much needed jobs and income. However, agriculture can be a high-risk sector, where the process of doing business – from farm to fork – may generate a variety of harms

to people and the environment. This includes salient impacts on human rights, natural resource depletion, and greenhouse gas emissions that increase climate risks, among others (see Figure 1 on common risk areas in agricultural supply chains and sourcing).

Launched in 2016, the OECD-FAO Guidance for Responsible Agricultural Supply Chains (OECD-FAO Guidance) describes common risks that can occur in agricultural supply chains and provides a globally applicable benchmark to implement responsible business practices. The OECD-FAO Guidance incorporates existing global standards such as the CFS Principles for Responsible Investment in Agriculture and Food Systems (FAO, 2014), the Voluntary Guidelines on the Responsible Governance of Tenure of Land, Fisheries and Forests, the UN Guiding Principles on Business and Human Rights and the OECD Guidelines for Multinational Enterprises (OECD, 2011).

The OECD-FAO Guidance is a global standard, building knowledge, capacity and awareness of development impacts when sourcing in global agricultural supply chains. It also introduces a risk-based due diligence framework to support mitigation of identified risks. In itself, due diligence is the process whereby companies identify, assess, mitigate, prevent and account for actual and potential risks according to the likelihood and severity of adverse impacts in business operations, through their supply chains and in business relationships.³ In tailoring business models to respond to risks and adverse impacts, companies can also support the Sustainable Development Goals by ensuring their operations are not undermining development objectives (OECD and FAO, 2016, 2020).

According to the United Nations Department of Economic and Social Affairs (UN DESA), the world's population is projected to grow to about 8.5 billion in 2030 and 9.7 billion in 2050, peaking at 10.4 billion in the 2080s (UN DESA, Population Division, 2022). Global demand for food will continue to rise to sustain this growing population. However, the adverse effects related to global demand for food can already be seen in a number of low- and middle-income countries, especially those which export globally traded commodities. In

² Responsible business conduct (RBC) is defined as the way in which enterprises can: a) make a positive contribution to economic, environmental and social progress with a view to achieving sustainable development and b) avoid and address adverse impacts of their own activities and prevent or mitigate adverse impacts directly linked to their operations, products or services by a business relationship (OECD and FAO, 2016).

³ For more background on due diligence, see page 21 in the OECD-FAO Guidance for Agricultural Supply Chains (OECD and FAO, 2016).

response, many governments have advanced sustainability, transparency and supply chain due diligence requirements that encourage enterprises to do more to reduce development impacts in global sourcing. This includes legislation designed to regulate the import of products linked to issues such as deforestation, forced labour and child labour in agricultural supply chains.⁴ The OECD-FAO Guidance – which since 2016 has been referenced in the policies and initiatives of over sixty governments, in addition to the European Commission, G7 and G20 – is among the leading instruments and standards

introduced to guide risk-based due diligence efforts. Beyond governments, many companies themselves are also issuing sustainability pledges to reduce and eliminate hazards in their supply chains. In 2021, references to the OECD-FAO Guidance in company policies, reports, and statements increased by 144 percent from the previous year (FAO, internal research, 2021). These developments point to the growing prioritization of RBC and environmental, social and governance (ESG) approaches among companies when considering sourcing strategies in agricultural supply chains.

Figure 1. Common risks in agricultural supply chains and sourcing



Source: OECD and FAO, 2020.

Competitive advantage and cooperatives

Corporate sustainability regulations and pledges frequently originate downstream, which can make implementation and compliance for upstream producers a challenge. This is particularly the case among companies, including small- and medium-size enterprises (SMEs), in developing countries that may not have the knowledge and resources to address risks in business operations on top of systemic development issues, such as poverty and corruption. To fulfil these commitments, companies

and key global traders need to consider practical ways to help producers build capacity to meet their supply chain responsible sourcing expectations.

Risk-based due diligence can help companies identify and support more inclusive and sustainable business relationships. Companies that are able to better manage and reduce negative development impacts in their supply chains can reduce the risk and cost of potential conflicts, litigation and remediation. Further, companies may receive reputational benefits, especially as RBC becomes

⁴ A non-exhaustive list includes the EU Directive on Corporate Sustainability Due Diligence (2022); EU Proposal for a regulation on deforestation-free products (2021); German Act on Corporate Due Diligence in Supply Chains (2021); Norwegian Transparency Act (2021); France Duty of Vigilance Act (2017).

a more mainstream requirement in trade and global markets. For agricultural cooperatives, strengthening due diligence measures can improve their standing as preferred suppliers among downstream companies and traders looking for partners whose values and missions align with their own and help them meet compliance obligations. Due diligence can also support cooperatives seeking opportunities to engage in agri-food value chains by aligning with global standards on sustainable agricultural production.

There is a growing body of resources available on how enterprise sustainability and responsible business conduct can be used as a management framework to advance competitive advantage and development. John Elkington's "triple bottom line" (1994) is among the earlier approaches that sought to integrate ESG elements in management and business models. It is based on three pillars: people, the planet and profit. Elkington's central idea argued that businesses who only consider a material focus on profits will overlook social and environmental consequences, and thus underrate the full cost of doing business.⁵ Conversely, Porter and Kramer (2011) introduce social and environmental externalities into the cost of business through an "ecosystem of shared value" that encourages competitiveness through business models that consider how to solve local challenges as a central part of corporate strategy. They argue that companies and communities can create *shared value* when business and management models align with societal needs. For the agricultural sector, such management approaches can support companies in their sourcing strategies with agricultural communities that often struggle with poverty.

Characterizing agricultural cooperatives

Cooperatives are an integral part of the global economy. In 2017, they provided direct and indirect employment to almost 10 percent of the global population (Möller, Davila and Esim, 2019). In the agri-food sector, their importance is more pronounced. Of the approximately 3 million cooperatives in the world, 1.2 million – or

40 percent – are agricultural cooperatives (ICA, 2018; NCBA CLUSA, 2022). They also play a key role in domestic markets and local economies. In Kenya, for instance, cooperatives were responsible for 22.2 percent of sales of agricultural products in 2019, including coffee, sugar and milk (Kenyan National Bureau of Statistics, 2020). Based on 2020 data, agricultural cooperatives in Vietnam directly contributed an estimated 4.8 percent to national gross domestic product (GDP) and over 30 percent indirectly through cooperative member households' increased income (Hanoi Times, 2020). As such, cooperatives can be important pillars of agricultural development and rural farmer livelihoods in low- and middle-income countries.

Agricultural cooperatives are based on a business model where a network of farmers, agri-processors, and others involved in production unite to conduct business as a collective unit to enhance the chance of success in domestic, regional and/or global markets by aggregating output and resources rather than tackling business individually.⁶ As such, they are economic actors with a goal of generating profit while helping producers obtain resources and services they may struggle to access individually, such as access to inputs, machinery, credit, or other value chain functions including marketing, packaging and transportation. A 2014 study in Ethiopia found that agricultural producers that were part of a cooperative were 5 percent more efficient⁷ than non-members due to the availability of technology and extension support services (Abate, Francesconi and Getnet, 2014). These services can create an enormous difference in reducing costs, increasing productivity and building capacity of farmers to enhance production and output (discussed below). Importantly, as agricultural cooperatives in developing countries are situated one tier above the producer-level – where environmental or social impacts can often occur – they are positioned to mitigate production-related risks and development impacts in agricultural supply chains.

⁵ Also see Elkington's 1999 book *Cannibals with Forks: Triple Bottom Line of 21st Century Business*. Oxford: Capstone Publishing.

⁶ The International Cooperative Alliance (ICA) has established certain principles typical of cooperatives, including voluntary and open membership; democratic member control; member economic participation; autonomy and independence; education, training, and information; cooperation among cooperatives; concern for community. Though not universal, these principles are widely recognized as key characteristics of cooperatives. See ICA.Coopoperative.identity.values.&.principles (2018).

⁷ Productive efficiency measured as the ability to obtain maximum possible outputs from a given set of inputs (Abate, Francesconi and Getnet, 2014).

Extension and training

In considering poverty and development, extension services, training and capacity building are among the most important services cooperatives offer. Providing information and resources on technical areas that can encourage better yields, sustainable agroecology practices, and access to markets is a core part of a cooperative's mandate to its members. Table 1 introduces some of the areas where cooperatives often provide agricultural value chain, business operation and financial support services to its members. These extension and learning services can boost farmer productivity, trade

opportunities and development outcomes. The case of the COOPCAB coffee cooperative in Haiti is one example, where technical assistance on coffee cultivation and pest management helped members reduce crop yield losses from 65 percent in 2009 to 15 percent in 2011, thus strengthening resiliency against insect plagues and disease (Root Capital, 2013). Such instances illustrate how cooperative extension services can equip farmers with necessary skills to meet trade and production needs amid changing externalities that can affect markets. Such changes can range from environmental and climactic shocks to new business and production-related regulatory requirements.

Table 1. Sample agricultural extension services offered by agricultural cooperatives

SERVICE CATEGORIES	EXAMPLE SERVICES
Agricultural value chain services	<ul style="list-style-type: none"> • Input supply (e.g. seeds, fertilizer, fuel, agro-chemicals) • Postharvest storage, transport, processing and/or packaging support • Access to veterinary services and information on animal health • Information on agroecological practices (e.g. intercropping, soil management, sustainable irrigation composting, promoting crop and animal diversity) • Downstream marketing and distribution services
Business and inclusion services	<ul style="list-style-type: none"> • Financial literacy training • Business management training • Information and training on sustainability certifications, fair labour practices • Information and support on markets, prices, trade, and regulations • Women's leadership training and information on gender equality • Access to legal services
Financial services	<ul style="list-style-type: none"> • Access to micro-finance institutions, mobile lenders and formal banks • Access to savings and credit cooperatives • Digital finance information and resources • Access to insurance services and brokers

Source: Adapted from FAO, 2022; Teague, 2015; USAID, 2019.

On social impacts in agricultural production, training can help cooperative members develop strategies to improve labour conditions and reduce adverse risk among informal, seasonal and migrant workers. Education on issues such as worker protection, forced labour and dispute settlement mechanisms can facilitate the introduction of business methods to respond to various instances in labour contracting and forecasting among member operations. For instance, to reduce conflicts between member farmers and their outsourced workers resulting from breaches in verbal contracts and unclear labour expectations, the Kuapa Kokoo cocoa cooperative in Ghana developed a project in 2015 to introduce written

contracts between members and hired workers. These contracts define the terms of agreement and safeguard the rights of hired workers, thus establishing more secure employment for workers. As of 2021, 1758 contracts had been signed (Divine Chocolate, 2022). Additionally, the project facilitates the creation of cooperative member committees that are trained on labour rights to build awareness of the project in their communities, assist with records management of signed contracts and mediate disputes between workers and farmers. By the end of 2021, 85 percent of all recorded disputes had been resolved (Divine Chocolate, 2022). Programs such as this demonstrate how cooperative services can reduce the

risk of worker mistreatment among informal workers and promote stable employment and decent work throughout the cooperative. By strengthening member capacity to address and mediate risks, cooperatives can be an effective partner for downstream companies that often lack visibility and influence in upstream agricultural sourcing communities to foster responsible business practices.

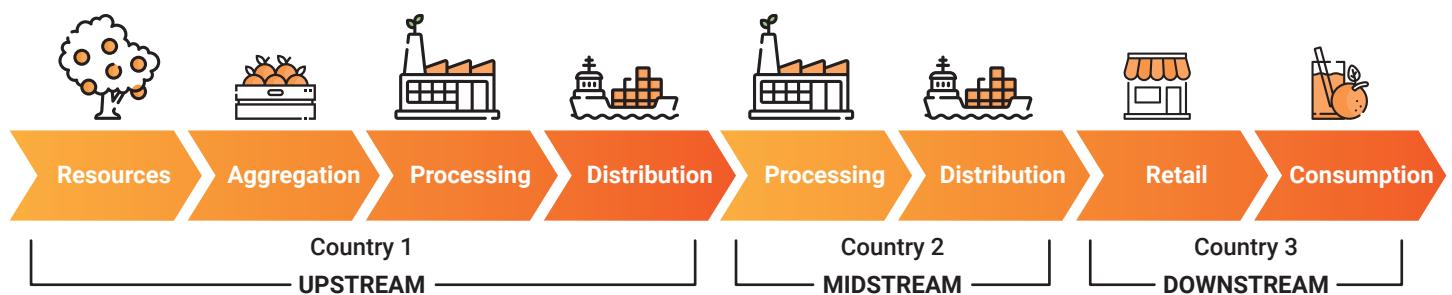
In many instances, cooperatives can build knowledge and capacity to address critical development risks and challenges in low- and middle-income countries. When considering environmental and social risks in agricultural production and sourcing, these existing challenges must be addressed. For example, in country contexts and agricultural sourcing communities where child labour is prevalent, cooperatives can provide services to help members address the issue, tailored to local development needs and downstream regulation on due diligence. In turn, results of these services can be communicated to buyers. The CAKHS cocoa and coffee cooperative in Côte d'Ivoire, with support from the ILO, provided members with training on how to identify cases of child labour and implement actions to eliminate them,

including providing access to basic education and vocational training. The programme resulted in the reduction of over 1800 children from hazardous work between 2010 and 2014 (ILO, 2014). As cooperative members often include networks of farmers, they are well-positioned to identify and build capacity to address root development challenges, like access to education, that are critical to consider in business risk mitigation strategies.

Global value chains (GVCs) and agricultural cooperatives

Global value chains are the series of stages of production of a commodity or service that cross at least three country borders. As a commodity moves through each stage of production, value is added through activities like cleaning, processing, refining, packaging, storage, marketing etc. to deliver the commodity from farm to table. These functions are also referred to as the upstream, midstream and downstream segments of agricultural supply chains (Figure 2).

Figure 2. Sample global value chain dynamics



Source: Adapted from FAO, 2020.

Estimates suggest that GVCs account for almost 50 percent of global trade across all sectors (World Bank, 2020). In agriculture, approximately one-third of global agricultural and food exports are traded within GVCs (FAO, 2020). By fragmenting the stages of production, GVCs offer farmers, SMEs, and cooperatives in developing countries greater opportunity to specialize in certain activities of the supply chain. In selling a portion

or all their yield to a cooperative, farmers can benefit from aggregated output, which is often needed in GVCs to meet large product volume, quality and frequency requirements of downstream buyers or traders.

Emerging and developing countries are responsible for approximately one-third of global agri-food trade; increasingly, they are becoming leading actors in GVCs (FAO, 2020). Some may even be commodity

export dependent, or near export dependency.⁸ An example includes Côte d'Ivoire, where cocoa makes up approximately 50 percent of total agricultural exports and accounts for roughly 6 percent of the country's GDP (WTO, 2021). In these contexts, GVC participation can be a dominant feature of the agricultural economy and thus an important source of income for SMEs, traders, producer cooperatives and other agri-sector workers. There is also evidence that GVC participation can result in higher incomes. Estimates suggest that a 1 percent increase in GVC participation can boost per capita income by more than 1 percent, much more than the 0.2 percent income gain from standard trade (World Bank, 2020). This can be seen in a 2018 study analysing the floriculture sector in Ethiopia, which found that workers in Ethiopia's export-focused fresh cut flowers sector earn significantly more than others engaged in standard trade sectors, largely because flower farms require a fixed group of workers to sustain supply to the global market (Suzuki, Mano and Abebe, 2018). Cases such as this illustrate how GVCs can both support economic growth and improve rural livelihoods in developing countries.

There is also evidence that GVCs can advance labour market opportunities for women. In developing countries, women make up 33 percent of the workforce of exporting firms across sectors, compared to 24 percent of non-exporting firms (World Bank and WTO, 2020). This figure can be more pronounced in certain commodity supply chains and have transformative effects in sectors that already employ a high percentage of female workers. In the banana sector, up to 45 percent of workers and small producers in the Caribbean are women (BananaLink, 2022), whereas in the Kenyan floriculture sector, women constitute approximately 75 percent of the workforce (Barrientos and Dolan, 2006). Further analysis illustrates that women's participation in the floriculture and tea GVCs in Kenya resulted in more stable job opportunities and permanent contracts, allowing for greater financial security (Said-Allsopp and Tallontire, 2014). In turn, this allowed women to increase their own financial independence and earn enough to purchase items such as land or livestock (Said-Allsopp and Tallontire, 2014). Advancing opportunities for

women in agricultural supply chains through responsible sourcing can facilitate economic and social development and decrease inequality.⁹

While both companies and development practitioners increasingly consider GVCs as a method to promote development, particularly through responsible sourcing strategies, this progress has evolved over time. Downstream trade requirements have shaped business relationships between suppliers and buyers in GVCs over the past several decades. A leading example includes the changing nature of standards and regulations governing fresh vegetable trade between Kenya and the United Kingdom of Great Britain and Northern Ireland (United Kingdom). Up until the mid-1980s, fresh vegetable exports from Kenya to the United Kingdom were mostly focused on meeting trade and production needs (Dolan and Humphrey, 2000; Gereffi, 2018). By the mid-1980s, lead companies, traders and retailors in the United Kingdom gradually began to introduce more stringent food safety and quality criteria on pesticide residues, post-harvest handling, as well as on environmental and labour standards of fresh vegetable imports. In turn, agricultural producers in Kenya – the largest supplier of fresh vegetables from Africa to the United Kingdom at the time – had to adapt to meet these changing downstream requirements. To ensure compliance, downstream traders and retailers became more involved in upstream production and processing segments of the supply chain. This included the introduction of procedures for growing, harvesting, processing and transport, regular exchange of information with suppliers, and monitoring adherence to standards through audits and inspections of importers, exporters and farms. As a result, the market dynamic between Kenyan suppliers and buyers in the United Kingdom adapted to meet downstream needs on sustainable production, food safety and responsible business practices. Such instances can be considered as precedents to today's sustainability standards that play an important role in global agricultural trade and business.

⁸ The United Nations Conference on Trade and Development (UNCTAD) define commodity export dependence in instances when more than 60 percent of a country's total merchandise exports are composed of commodities. See UNCTAD, 2021.

⁹ For more information on how companies can support gender equality by integrating a gender-responsive risk-based due diligence in agricultural supply chains see: OECD and FAO, 2016.

Sustainability standards and certification

In the agricultural sector, sustainability standards and certifications are designed to ensure that food and agricultural products are produced, processed and/or transported in line with specific economic, social, and environmental sustainability criteria, including respect for basic human rights, worker health and safety, the environmental impacts of production and others (UNCTAD, 2020). Voluntary standards and certifications are commonly used by producers, traders, retailers and other agri-food actors as mechanisms to advance and demonstrate their commitment to more ethical production and sourcing. Though they share some overlapping goals and objectives, sustainability standards differ from international food quality or food safety regulations, such as the World Trade Organization's Agreement on Sanitary and Phytosanitary (SPS) measures. In many cases, sustainability standards and certifications are voluntary. However, some of these voluntary measures are increasingly included in supply chain due diligence regulations. The OECD-FAO Guidance, which has been introduced in certain legislation as a framework for responsible business conduct in the agricultural sector, is one specific example (see discussion above). Consequently, sustainability standards and certifications have become closely intertwined with global initiatives on responsible sourcing and sustainable food systems.

The growth of GVCs has facilitated the rise of sustainability certification standards, driven by lead companies that seek assurance and credibility on the environmental and social impacts of sourcing, production and processing methods across different markets and supply chains. This can be seen through the mushrooming of voluntary standards and certification labels in recent decades. Some estimates suggest there are over 400 sustainability standards globally across a range of sectors (IISD, 2022). As of 2022, there were over 160 active standards for the agricultural sector that aim to regulate a range of risks in various countries, commodity supply chains, and stages of production (ITC, 2022).

Demand for responsibly grown food and agricultural products from both consumers and downstream buyers has also facilitated the growth of sustainably certified products in retail markets. According to a recent study, sustainability standards and certifications operating in at least four agricultural commodity sectors — bananas, coffee, cocoa, and cotton — captured close to 10 to 15 percent of their respective markets in 2018 (Voora

et al., 2022). The increase in demand has had a clear impact on agricultural production. For example, the total certified area of cotton, cocoa, palm oil and coffee grew by over 50 percent between 2014 and 2018 (ITC, IISD, and FiBL, 2018). The prevalence of sustainability standards and certifications in agriculture will likely continue its upward trend alongside sustainability legislation and regulations.

Many agricultural cooperatives already have experience in integrating sustainability certification criteria among members to respond to needs of downstream retailers. One instance includes the business relationship between upstream cooperatives in developing countries and the food retailer, Co-op, the United Kingdom's largest seller of Fairtrade products. In 2012, Co-op adapted its business model to ensure all its bananas were Fairtrade certified and sourced from cooperatives, half of which worked directly with smallholder farmers (Fairtrade, 2022). In aggregating efforts to work with smallholders, cooperatives can serve as a platform to collectivize outputs, meet product volume requirements and build capacity on sustainability criteria, as in the case of Fairtrade certification. Likewise, the administration involved in certification can be burdensome and complicated for smaller producers, which cooperatives often assume as part of their responsibilities. An example includes Coocafé, a consortium of seven small and medium coffee cooperatives, representing about 2000 farmers in Costa Rica. Coocafé manages the Fairtrade certification process on behalf of its members, including arranging audits and coordinating with the Fairtrade certification monitoring body (Snider *et al.*, 2017). This managerial support is critical for small cooperatives that might otherwise lack human capital to navigate and comply with various steps of the certification process.

In cases where cooperatives lack financial capacity to carry out certification, financial support from other upstream actors, including buyers, can be essential. In 2022, five vanilla cooperatives in Madagascar, representing a total of 1791 farmers, were able to obtain Rainforest Alliance and organic certification with financial support from the vanilla exporter Ramanandraibe Exportation (RAMEX), in cooperation with the US spice company McCormick & Company and the United States Agency for International Development (USAID). For the companies, certification helped reduce the risk of biodiversity loss and natural resource depletion in communities involved in vanilla production and export. In turn, the cooperatives received a price premium of USD 223 200 from RAMEX for the

organic-certified product (USAID, 2021). Thus, certification and standards can give cooperatives the opportunity to gain higher prices for output, upgrade to more responsible business practices and drive those efforts downstream.

Though important to trade and development, sustainability standards and certifications cannot substitute for a comprehensive approach to risk-based due diligence. Sustainability standards and certification are highlighted in steps three and four of the OECD-FAO Guidance's five-step framework (discussed below). However, many downstream companies can

become reliant on certifications as a “check the box” approach to fulfil key performance indicators on ethical sourcing and sustainable development. A siloed use and focus on certification or standards may not allow for the identification, mitigation or prioritization of environmental and social risks that are most relevant to companies and tailored to their individual business models. Importantly, certification can be costly and inaccessible for many producer cooperatives (discussed below) or seen as statutory exercise rather than part of a comprehensive risk-mitigation strategy.¹⁰ More details of such challenges are included in Box 1 below.

Box 1. Gaps in sustainability certifications and due diligence

Sustainability certifications can provide a valuable framework of responsible business practices for smallholder farmers and cooperatives. They are an effective part of the larger due diligence process. However, on their own, they are not a sufficient tool to identify and mitigate the full range of environmental and social risks in a company's operations. Below are some examples of where sustainability certifications fall short of risk-based due diligence.

Certification rewarding compliance vs. incentivising responsible business practices

Low market demand for certified products, weak financial incentives and the high auditing and management costs of maintaining certifications can encourage cooperatives to certify only a portion of their members. This strategy rewards compliant farmers rather than stimulating widespread responsible business conduct throughout the entire cooperative membership (Snider et al., 2017).

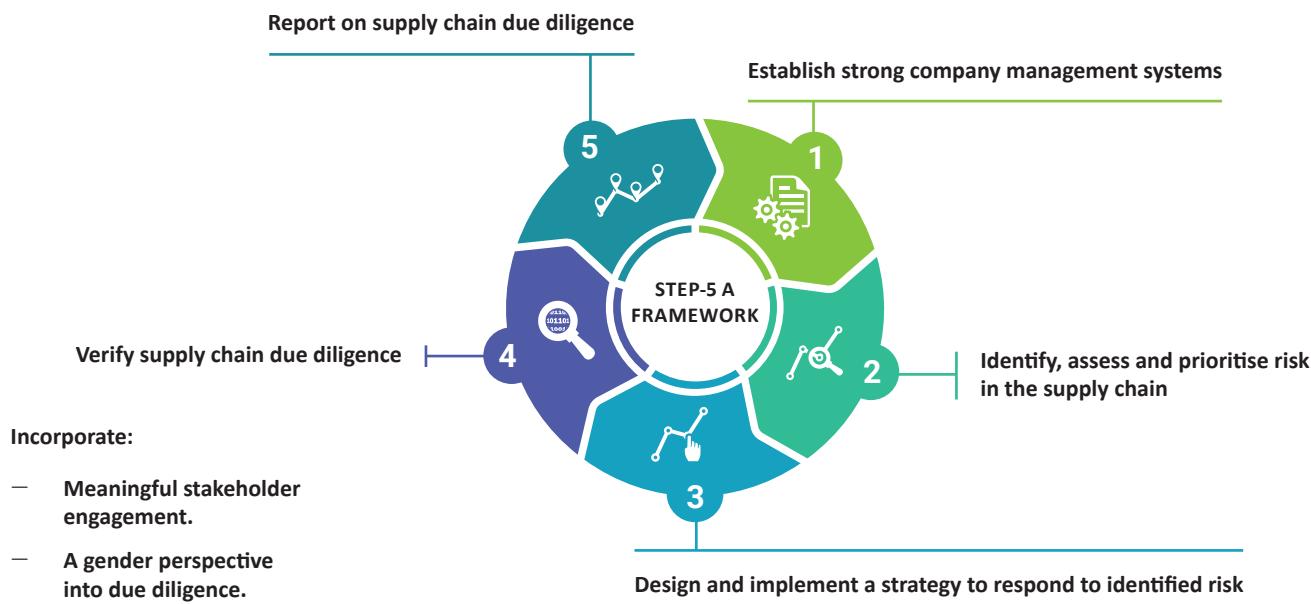
Narrow certification of a singular commodity

Farmers may produce several different commodities within their crop fields; however, many sustainability certifications are commodity-specific. These certifications narrowly account for environmental or social risks related to that product but may not be transferrable or applicable to other commodity sectors (Minten et al., 2018).

Lack of benefit-sharing between members and workers

The financial and social benefits of certification help cooperative members but may not trickle down to the farm workers that cooperative members employ, including landless farm workers, migrant workers and family members, etc. As labour standards on the cooperative member' farms may not be monitored during certification inspections, farmers lack incentive to uphold the same responsible business standards as the cooperative-level (Meemken et al., 2019).

¹⁰ Considerable effort has been made in recent years to the development of alignment assessments in order to enhance coherence among divergent sustainability standards. For the agricultural sector, this assessment seeks to evaluate how various industry or multi-stakeholder initiatives align with the recommendations of the OECD-FAO Guidance for Responsible Agricultural Supply Chains. Supporting alignment of these initiatives can facilitate consistency with government-backed standards on responsible sourcing and due diligence. For more information see: [OECD Alignment Assessments of Industry and Multi-Stakeholder Programmes and FAQ responsible business conduct in Agriculture](#).

Figure 3. Five-step framework for risk-based due diligence

Source: OECD and FAO, 2016.

Many certification bodies themselves seem to be aware of the limits of the scope of their certification products or services. For example, the Rainforest Alliance and Fairtrade International publicly acknowledge that certifications are not enough to address human rights issues in global supply chains and meet compliance expectations regarding risk-based due diligence.¹¹ Sustainability standards and certifications can complement, rather than replace due diligence and responsible sourcing efforts. For cooperatives, adopting a broader approach to risk and development is critical to increase competitiveness and visibility as credible suppliers in global value chains.

Agricultural cooperatives and due diligence

Due diligence is an on-going, proactive, as well as reactive package of steps. The process helps actors move from identifying environmental and social risk to implement steps to prevent and mitigate risk, as well as verify due diligence actions and report on progress. This section outlines examples of how the five-step framework of the OECD-FAO Guidance (Figure 3) can be adapted for agricultural cooperatives. By implementing the OECD-FAO risk-based due diligence framework, cooperatives can foster a positive culture around risk mitigation in business conduct among members and better position themselves to access and participate in GVCs.

¹¹ See The Rainforest Alliance, *The Need For Due Diligence Legislation* (2019); and Fairtrade International's *Vision for Human Rights and Environmental Due Diligence* (2020) statements.

► Step 1. Establish strong enterprise management systems for responsible supply chains

Strong cooperative operations should be built through a well-rounded management system that communicates the norms, policies and practices the organization is committed to when considering environmental and social impacts among members. As part of this system, cooperatives should adopt or integrate into existing policies a single or set of policies on RBC. The policy can address common risks agricultural cooperative members may be exposed to. It should illustrate the cooperative's comprehensive efforts and commitment to support members in reducing environmental and social risk. Cooperative management or a designated cooperative member may be responsible for monitoring and oversight of the RBC policies and due diligence process. Understanding the prevalence of sustainability certifications for cooperatives, the policy may reference adherence to any certifications or standards that are used to support the implementation of this policy. However, the responsibility to conduct due diligence rests with the cooperative itself, not certification bodies or other downstream partners.

Ensuring inclusiveness is critical where policies can be developed together with different stakeholders that may be engaged in or impacted by cooperative operations, including individual cooperative members, hired workers, women, youth, ethnic groups and Indigenous Peoples. Moreover, education, training and capacity building on the RBC policy can be coordinated through various levels of cooperative participants, including cooperative management and NGOs. Finally, the policy should be communicated and incorporated into contracts and agreements with partner organizations and other relevant business relationships to set expectations of responsible conduct.

► Step 2. Identify, assess and prioritize risks in the supply chain

To understand the actual and potential negative impacts of business conduct, cooperative management should conduct a broad scoping exercise to map business operations and risks among its members. If possible, maintaining written or digital records on the name and nature of member business operations (e.g. crops produced, location and sources of production, contextual

information of producing regions like water stressed areas, conflict zones etc.), and any information that is feasible to gather, such as the number of hired workers on member plots (contract and/or informal), the breakdown of workers by gender, age, and transportation routes, can be useful to monitor developments and potential risks as they arise and reported to downstream partners and companies.

In a risk-based model, due diligence prioritizes the identified hazards based on the severity and likelihood of the adverse impact. For example, in its 2021 sustainability report, Dutch multinational confectionary company Tony's Chocolonely disclosed 1 701 identified cases of child labour in its supply chain, all of which were occurring among the company's newest cooperative partners, indicating priority area for risk remediation efforts (Tony's Chocolonely, 2021).

Risk assessments must be done in consultation with members, workers and other stakeholders such as NGOs and local/regional government (including labour inspectors) who are familiar with risks in the local agricultural production context. Risk assessments may also be financially and/or logically supported by trade unions, larger cooperatives, or sponsored by downstream actors. Downstream business partners should understand the risks producer cooperatives face to ensure that the terms of business are favourable, fair and sustainable.

► Step 3. Design and implement a strategy to respond to identified risks

Together with its members and partners, a cooperative should develop an action plan that responds to the identified and prioritized risks. For example, if a cooperative and its members identify a scarcity of freshwater resources that impact the availability of water for farming, a strategy to introduce ways to improve efficient use and saving of freshwater resources through modern irrigation techniques or other solutions designed with members. If and where technical support is needed, development partners such as NGOs can work with cooperatives to implement new techniques to preserve or reuse water resources in production.

For downstream companies – including traders and other enterprises sourcing from agricultural cooperatives – it is critical to understand the capacity of cooperative operations to ensure sourcing strategies are not

contributing to adverse impacts. Companies could provide technical support to help cooperatives where there are gaps in risk mitigation needs and capacity. For example, in the case of Tony's Chocolonely mentioned above, rather than terminate the business relationship with cooperatives that employ child labour, Tony's Chocolonely works with them to implement strategies to address root causes of hazardous risk, like providing wheelbarrows to prevent heavy lifting and organizing bicycles for transport to and from school.

► Step 4. Verify supply chain due diligence

Cooperatives should develop and coordinate verification mechanisms to monitor and track implementation and effectiveness of risk mitigation/prevention strategies among members. Cooperatives may develop their own verification mechanisms together with other actors to meet local needs and conditions. For instance, the OECD-FAO Guidance references the Sustainability Initiative of South Africa's (SIZA) programme to devise a unifying set of social and environmental standards for South Africa's fruit producers, based on domestic laws, the Global Social Compliance Programme and ILO conventions (OECD and FAO, 2016). If resources permit, cooperative management could appoint focal staff responsible for periodically monitoring progress, implementation and outcomes of verification efforts among members. As previously mentioned, the use of audits or certification schemes may support verification efforts but should not be relied on as the sole means of

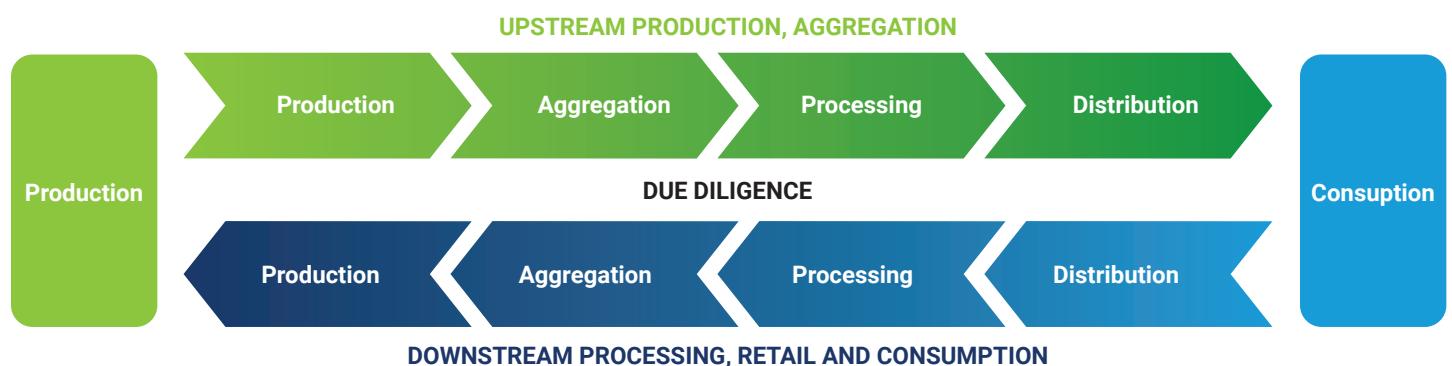
due diligence. The due diligence process goes beyond audits and such investigations may not be effective in identifying the full set of risks outlined in the OECD-FAO Guidance. Value chain actors that source from or partner with agricultural cooperatives can consider providing financial or technical support in the verification process as needed.

► Step 5. Report on supply chain due diligence

Communicating the findings and outcome of the due diligence process is the final step of the framework. As a member-driven organisation, communication is a critical component of cooperative operations. Reporting on risk-reduction efforts can be built into regular updates and communications with cooperative members via email, flyers, social media or other accessible outlets. Biannual or quarterly updates are recommended, if feasible. The report should be populated with information on identified risks, steps taken and measured progress in risk mitigation based off the previous four steps of the five-step framework.

This information should also be promulgated through the chain to buyers, NGOs and other partners (Figure 4). Reporting on due diligence process can build trust and establish credibility among external partners that the cooperative makes a concerted efforts to reduce and eliminate negative social and environmental risks in business conduct.

Figure 4. Flow of due diligence information between actors in agricultural supply chains



Source: Authors' own elaboration, 2022.

Remaining challenges and way forward

This policy brief has assessed how agricultural cooperatives in developing and transitional economies provide important resources and capacity building services for millions of smallholder farmers, helping them increase access to and participation in GVCs. It finds that by providing members with access to knowledge, extension services and training that encourage responsible business conduct, cooperatives can provide leverage in efforts to reduce adverse development impacts of agricultural production in sourcing communities. Such services can be an effective tool to improve farmers skills to meet production and export needs, while addressing various risks and root development challenges that must be accounted for in supply chain risk mitigation efforts. Importantly, these benefits can strengthen agricultural cooperatives competitiveness in GVCs as a responsible supplier, and enable them to benefit from higher incomes, employment opportunities, and access to more sustainable modes of production. Overall, this can encourage better development outcomes for agricultural cooperative members and help lift rural agricultural communities out of poverty.

However, several challenges must be considered regarding the operational efficiency of agricultural cooperatives before introducing services to members on risk-based due diligence. The first and foremost includes whether a cooperative already trades in GVCs, and if not, understanding and considering the costs and benefits of tailoring its focus to export markets. While GVC participation has the potential to create new and increased revenue streams, it may not be a viable option for all cooperatives, especially in developing countries where limited financial and technical resources may need to prioritize local development needs such as climate change mitigation, adaptation and food security.

Next, strong management and functionality is key to cooperative sustainability and success. Studies have highlighted that in developing countries, effective management is often a leading factor in the operational efficiency of a cooperative, including its ability to participate and trade in GVCs (Francesconi and Wouterse, 2019; Francesconi, Wouterse and Birungi Namuyiga, 2021). This is also important to consider when assessing whether a cooperative can financially

govern and manage itself. In 2014, members of a coffee cooperative in Peru experienced severe challenges with their parent cooperative because of weak financial management, which ultimately obstructed cooperation and resulted in the inability of the cooperative to source enough coffee from its members to meet downstream demand (McCreless, 2014). Member trust in cooperative's ability to function eroded to the point where members began side selling their coffee to other local buyers rather than to the cooperative (McCreless, 2014). Side selling is a frequent problem for cooperatives, which takes place when a member does not comply with a contract and chooses to sell to other buyers. Further, ensuring effective management, along with support and loyalty of members to avoid issues like side selling can be a challenge for cooperatives. The ability of cooperatives to lead and introduce extension services, including those related to risk-based due diligence, may be considerably lower if members do not fully support their cooperative.

Finally, accessing finance is another critical challenge agricultural cooperatives in developing countries. For cooperatives that lack financial and technical resources to function effectively, introducing services and training on due diligence, decent work, natural resource management or other responsible business practices might not be a priority. This may particularly be the case for agricultural cooperatives that are not linked to global export markets, but rather geared towards subsistence farming or local trade, which may not be governed by the same sustainability criteria of downstream or global markets. Similarly, the high cost of qualifying for export-oriented sustainability standards can be a significant barrier for cooperatives. In Kenya's vegetable export industry, for instance, the cost of certification can be as high as 30 percent of a smallholder's annual vegetable income (Asfaw, Mithöfer and Waibel, 2010). This is a significant investment, especially for producers that may struggle to meet basic needs.

Key takeaways and recommendations

Build cooperative managers, employees and member knowledge on responsible business conduct, due diligence and market requirements

Increasing knowledge, awareness and capacity of agricultural cooperative managers, employees and members on what RBC and due diligence is – and how it relates to expectations and requirements of their customers and export markets – is an important step in developing training for members on risk-based due diligence. Disseminating information on environmental and social sustainability expectations may also help drive demand and incentivize participation in such programmes among cooperative actors that seek to comply with new and emerging market requirements.

Increase and enhance training and extension services tailored to the identification, prevention and mitigation of environmental and social impacts among cooperative members

Provision of training and extension services is one of the key benefits of cooperative membership for farmers. Deepening and expanding training to members on a range of responsible business practices and how members could benefit from their adoption, including collecting information on social and environmental impacts, risk-prevention methods, remediation activities related to identified impacts (e.g. child labour), respect for occupational safety and health, food safety standards and others can reduce development impacts.

Build the capacity of cooperatives to increase access to financial resources

Cooperatives need access to adequate financial resources to implement trainings on due diligence and adopt techniques to respond to identified risks. Thus, building the capacity of cooperatives to access and/or increase their financial resources is an important component of strengthening cooperative environmental and social risk mitigation efforts. In such opportunities, donors and other development partners must also consider trainings on financial management to ensure greater operational stability and sustainability.

Consider risk-based due diligence as a method to enhance business operations and competitiveness as a responsible supplier

Trade in GVCs is increasingly reliant on building a community of suppliers and actors that respect and adhere to responsible business practices. In strengthening their approach to RBC and due diligence, cooperatives are better placed to increase competitiveness and become a preferred supplier in supply chains. Cooperatives that demonstrate an understanding of development impacts and market needs have the opportunity to strengthen their own operations and better position themselves to trade globally.

Encourage supply chain risk mitigation efforts that go beyond certification

Responsible sourcing efforts must address a range of development risks that are specific to certain enterprises, countries, communities. This often goes beyond the scope of sustainability certification and standards. Rather, comprehensive and effective due diligence among cooperative members and downstream actors must be central to efforts to understand how to identify and mitigate risks in agricultural supply chains and promote inclusive growth in agricultural sourcing communities.

Support multi-stakeholder collaboration between upstream and downstream actors in agricultural value chains

Integrating considerations that address poverty and responsible business practices, while promoting inclusive business growth of cooperatives, requires concerted effort from many upstream and downstream actors. Multi-stakeholder platforms can help agricultural cooperatives in developing countries, companies, governments, financial institutions, NGOs and other stakeholders understand where and how sourcing practices, trade and/or development policies are contributing to adverse risks for agricultural cooperative members and their communities and provide a forum to develop strategies to reinforce risk mitigation and development needs.

Support efforts to promote an enabling environment for responsible business conduct and due diligence for agricultural cooperatives

On a broader level, efforts to promote an institutional, operational, and regulatory environment that is conducive to effective cooperative enterprises can be critical to ensure that agricultural cooperatives in developing countries can implement RBC and build competitiveness in GVCs. Governments, NGOs, international agencies, and other actors can help shape and promote effective public policies that support participation in cooperatives, uphold international labour standards, promote anti-corruption efforts, and reduce the risk of unfair competition and trade practices with other enterprises, among other issues.

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