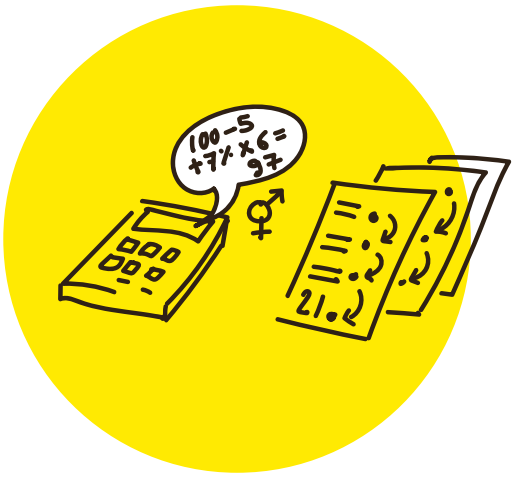
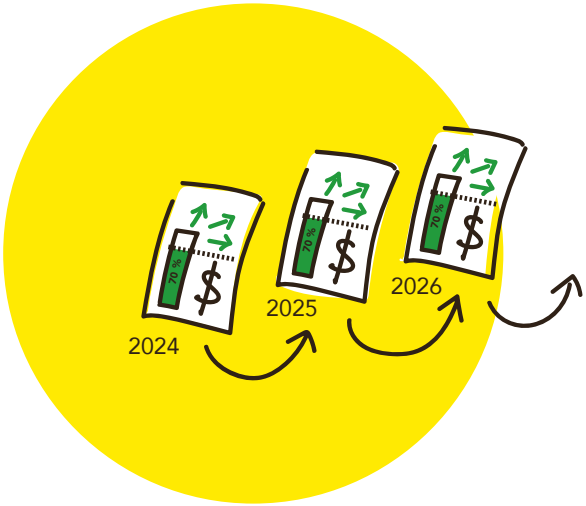
VOICE
www.voicenetwork.cc

# Good Purchasing Practices




**a cocoa barometer** consultation paper

# Good Purchasing Practices

**a cocoa barometer** consultation paper

## Introduction

*Many of the holistic interventions necessary in cocoa are long-term processes that will lead to change over time. However, (extreme) poverty is a daily reality for the vast majority of cocoa farmers. They cannot afford to wait until long-term processes – such as diversified income, higher productivity, or a better rural infrastructure – have come to pass. Many good purchasing practices do not require collective sector-wide action, nor do they require a long development process; they can be implemented on a relatively short term, by individual corporate actors.*

*It's not rocket science; if companies care about the poverty of cocoa farmers, they should pay farmers more. Besides fair pricing, the risk cocoa farming households face must be shared more equitably.*

*Concretely, companies must introduce the practice of paying living income reference prices at farm gate level, i.e. paying farm gate prices that would enable median farmer households to earn a living income from the sales of their crop. Similarly, companies must also provide farmers with long-term asymmetrical contracts (providing farmers more rights, while putting more responsibilities on the shoulders of the purchasing companies) and be transparent and accountable about their purchasing practices.*

**Three imperatives to achieve a living income**

Living income is a moral imperative, a business imperative, and a legal imperative.

Firstly, living income is a human right in and of itself. As such, Living Income deserves a centred position in any conversation around the changes needed from a rights-based perspective. Ensuring a living income is therefore a **moral imperative.**

In addition, farmer poverty is a driver of just about every other problem in the cocoa sector; deforestation, child labour, and gender inequality are all made so much harder to tackle if cocoa household incomes are not raised significantly. Providing a living income makes sense from a perspective of achieving Environmental, Social and Governance (ESG) targets. Furthermore, long-term sustainability also enables

greater security of supply: fair and sustainable value chains are future-proof. In that sense, ensuring a living income is therefore also a **business imperative.**

With several major sustainability regulations coming into force[1], the voluntary nature of tackling farmer poverty will soon be an idea of the past. Ensuring a living income for smallholders in the supply chain will also become a **legal imperative** within the foreseeable future.

## Business as usual

There is significant evidence that current approaches to raise farmer income have marginal impact at best. There is an insignificant correlation between higher productivity and net income. In some cases, there is even a negative correlation.[2] In fact, recent research shows that labour intensive approaches to alleviate farmer poverty – such as increased productivity or diversified production – lead to higher incidence rates of child labour.[3]

Nevertheless, most cocoa and chocolate companies continue to operate under a business-as-usual scenario: company programmes aimed at improving livelihoods are focused on higher yields, farmer training, and income diversification.[4] Moreover, company interventions more often than not take the form of pilots, placed next to or even outside the current supply chains of companies, and seldom target the buying practices of these same companies. With the notable exception of Tony Chocolonely's Open Chain approach, no large chocolate or cocoa companies are paying higher prices at farm gate level – whether through a direct farm gate price or through premiums high enough to offset compliance costs. The companies' purchasing divisions strive to buy cocoa as cheaply as possible, and farmer poverty is not taken into consideration in their daily practice.

Under normal circumstances, this would already be severely problematic. However, the Covid 19 pandemic and the war in Ukraine have triggered a cost-of-living crisis in West Africa, where most of the world's cocoa is grown. This is further exacerbated by severe inflation in Ghana, the world's second biggest cocoa producer.

## Current market dynamics

Though at present world market prices are temporarily at high levels, this is primarily due to bad harvests caused by the El Niño weather pattern. As soon as El Niño is over, the market is expected to be back at a structural oversupply, and therefore structurally low prices.[5] At present, market actors are baulking at the high prices.

---

1 In 2023, the European Union's Deforestation Regulation and the German *Lieferkettengesetz* came into force, the EU's Corporate Sustainability Due Diligence Directive is expected to be introduced in the course of 2024, the French *Loi de Devoir de Vigilance* has been in place for several years, and several other countries in major cocoa consuming regions are developing supply chain regulations.

2 For example, the 2021 IDH Farmer Field Book Analysis report of some of the major cocoa and chocolate company's projects on fertiliser use shows that there is no positive correlation between higher productivity and net income. And in some cases, it shows there is a negative correlation. Oxfam recently did a study in Ghana with similar outcomes.

3 See this recent study by the Royal Dutch Tropical Institute (KIT).

4 An earlier draft of this paper was shared with several cocoa and chocolate companies. Several stated that one of the reasons that some of these interventions failed, was because the targeted productivity increase wasn't achieved. As we have written in the Living Income Compendium and in the 2022 Cocoa Barometer, if there is no business case for higher productivity, farmers are not incentivised to spend the time and risk to increase yields. This business case is made by a combination of decent infrastructure and governance on the one hand, and on good purchasing practices on the other. If the purpose of projects is to raise productivity, higher prices are likely to be a very effective tool to achieve that purpose.

5 ICCO World Cocoa Market Forecast September 2023.

Furthermore, farm gate prices in Côte d'Ivoire and Ghana – the world's two largest cocoa producing nations – are set through a forward selling controlled system. Though this reduces risk in the case of downward price shocks, it creates a 12-to-18-month delay from the world market. The lack of transparency in this forward selling system also leads to lower farm gate prices[6]. As such, farm gate prices in the two leading cocoa producing nations are lower than the current world market.

**Good harvest**
**Low prices**

**Bad harvest**
**High prices**

### United Nations guiding principles on business and human rights

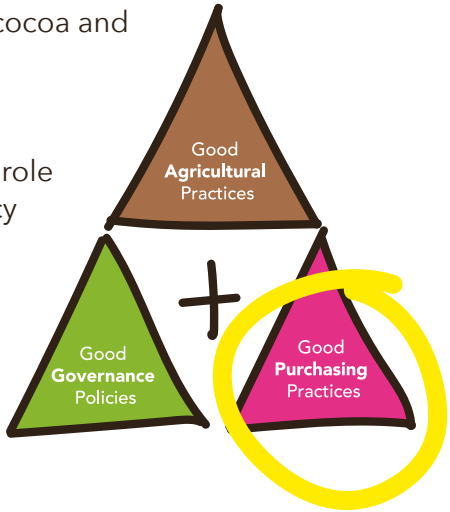
The United Nations Guiding Principles on Business and Human Rights clearly state that the corporations' responsibility to protect human rights "exists independently of States' abilities and/or willingness to fulfil their own human rights obligations and does not diminish those obligations". In other words, even when governments are not doing what they should, this cannot be an excuse for companies not to do what they can.

### Good purchasing practices

The current world market system is designed to make the weakest link in the supply chain – smallholder farmers – compete among themselves, driving prices down and risks up. Civil society organisations have been insisting for decades on the need for companies to pay better prices at farm gate, therefore requiring them to engage in good purchasing practices[7]. However, the industry often resisted discussion on how their purchasing practices are affecting farmers in their supply chains. Recently, as the topic has been gaining traction, there has been a noticeable shift in the cocoa sector: from resistance, the response is moving more towards 'how?'[8] This consultation paper is an attempt to outline what these good purchasing practices could and should look like for cocoa and chocolate companies.

### Scope

There is a lot to say about the role of terminal markets, the role of governments in rural development policies, transparency of taxes and investment, the importance of supply management, as well as the role of the financial sector in providing credit systems. There is also a lot to say about the importance of good agricultural practices, and the efforts farmers themselves can make to increase their net income.




6 In years of low prices, this price stabilisation is generally regarded as a boon to cocoa farmers. However, there is not enough transparency and accountability by the Ivorian and especially Ghanaian cocoa boards in how these prices are set.

7 See also the 2022 Cocoa Barometer and the 2022 Living Income Compendium.

8 An earlier draft of this document was shared with several cocoa and chocolate companies. One company stated that it was 'a stretch' to say 'for decades', "given that it is only in the past twelve months that this topic has really come to the forefront." We are happy that companies are starting to listen to the call, but that does not mean the call is recent.

Only focusing on price will not solve the issue, in the same way that only focusing on e.g. supply management, development policies, or yield gains is equally insufficient. Holistic approaches are needed: approaches that look at governance policies, Good Agricultural Practices, and purchasing practices. Within that context, cocoa and chocolate companies are so far sorely lacking in tackling their responsibility for their own purchasing practices.[9] This paper deals specifically with the purchasing practices of companies at farm gate and farmer cooperative level.

Though the majority of the examples in this paper will focus on the situation in the two largest cocoa-producing countries, Côte d'Ivoire and Ghana, the principles around remuneration, risk, and accountability are the same regardless of sourcing area. In fact, these principles would largely be appropriate to most agricultural production regardless of crop and country.

**Sphere of control**

Often, companies complain that civil society asks are about topics that are outside of their control or even outside of their sphere of influence, such as government policies. However, the way in which companies buy their ingredients is 100% within their sphere of control. The living income gap for the cocoa sector is around $10 billion dollar per year[10]. Though this is a large sum, chocolate companies give their stockholders far more.[11]

**Purchasing - not sustainability programmes**

Some approaches take a broad view of purchasing practices, to include topics such as value distribution, freedom of association, collective bargaining, and worker organisation, as well as investments in community building and infrastructure. These are important topics that need to be addressed, to be sure. However, after twenty years of the cocoa sustainability debate focussing on programmes, it is important that we also address the core business of cocoa and chocolate companies, which is the buying and selling of cocoa products. It is in this core business that purchasing practices need to change, which is why we are focusing on that in this paper. Within the context of sustainability, it is important that purchasing practices focus on the impact on the farmers, not just on the compliancy efforts of the multinational: rather than looking at whether there is a change in how a company does procurement, companies should be looking at whether the farmer is actually being helped through lower risks and higher prices. Responsible purchasing practices are about supporting farmers in their ability to earn a living income from their core business.

**Immediate impact of purchasing**

While many of the programme/development-based approaches described above are important, their impacts are often on the longer term. Companies that improve the purchasing practices in their supply chain can have immediate and highly significant impact, both individually and collectively. Moreover, sustainability programmes and development-based approaches are heavily impacted by

---

9 The entirety of chapter 8 of the 2022 Cocoa Barometer goes into depth into the relationship between Good Agricultural Practices, the role of governments in ensuring Good Governance Policies, and the responsibility of companies to engage in Good Purchasing Practices (pp 106 and further).

10 Kiewisch, M., & Waarts, Y. R. (2020). *No silver bullets: Closing the $10 billion income gap in cocoa calls for cross-sector action.* Wageningen Economic Research.

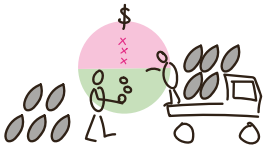
11 The Ferrero family pays itself an annual dividend of up to half a billion euros per year. Between 2014 and 2020, the Mars' family wealth increased from $60 billion USD to $94 billion USD. Between 2010 and 2020, Nestlé bought back $46 billion USD in shares. Living Income Compendium, 2022, p 11.

farmer poverty, and as such require good purchasing practices for their effective implementation.

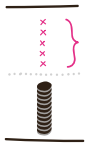
**Three elements of purchasing practices**
Companies wishing to implement good purchasing practices must address three separate elements: **remunerative prices** (building on the core of a farm gate price that is sufficient for a living income), **risk sharing** (including long-term asymmetric contracts), and **transparency and accountability** (public communication by companies that can be independently verified).

This paper explores these three elements in more detail, provides suggestions for companies on how to start, and raises further questions for exploration. Where possible, the paper outlines suggested purchasing practices for both traders with direct relationships to farmer cooperatives, as well as to brands that operate further downstream in the supply chains. Where necessary, these recommendations are adapted to national circumstances for the two major cocoa-producing nations, Côte d'Ivoire and Ghana.

Good purchasing practices, quite simply, are **remunerative prices**, at **acceptable risk**, **transparently communicated**.



**Farmgate prices paid ...**



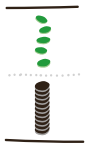
**Living Income gap**

Current prices

**... are too low to make a living income**

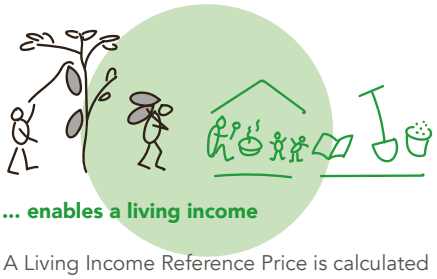
**A Living Income Reference Price ...**

A living Income Reference Price (LIRP) is a farm gate price that is sufficient to bridge the living income gap for an average cocoa farming household.



**Living Income Reference Price**

Current prices

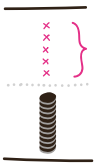


**... enables a living income**

A Living Income Reference Price is calculated based on the household needs - including costs of labour, inputs, etc. and supplements the going farm gate price with additional payments (such as premiums) when necessary.

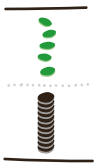
# Remunerative price

In many commodities there is a gap between what farming households actually earn and the level of income they need to achieve a living income.[12] This is called the living income gap. Any cocoa or chocolate company that is serious about bridging this gap needs to ensure its efforts are aligned with its purchasing practices.



**Living Income gap**

Farm gate price



**Living Income Reference Price**

Farm gate price

## Living Income Reference Prices

The core of any good purchasing practices is a farm gate living income reference price (LIRP). The principle of a LIRP is that the base farm gate price[13] is supplemented by additional payments direct to farmer that bridge the remaining living income gap. This LIRP should be the outcome of a calculation of realistic variables such as cost of production, yield per hectare, farm size, other sources of income, household size, and the relevant living income benchmark. The level of a LIRP should be regularly

12 All of the major cocoa-producing nations have regularly updated living income benchmarks, which are made available on the website of the Living Income Community of Practice.

13 The farm gate price often differs from the world market price set at the terminal markets. This chapter deals with the price paid at farm gate, not the world market price or other prices that are set further downstream in the supply chain.

reviewed and amended when circumstances change.[14] Though there are differences between various living income reference price calculations, it is clear that without implementing a reference price, companies cannot claim sustainability, because they simply don't know if their farmers are forced into poverty pricing.

A living income reference price is a farm gate price that is sufficient to bridge the living income gap for an average cocoa farming household. It is calculated based on actual household needs and supplements the farm gate price with additional payments.

**Liberalised and regulated markets**

In many cocoa-producing countries, there is a liberalised market and farm gate prices change from day to day. In the two biggest cocoa-producing countries, farm gate prices are set once or twice a year through national cocoa marketing boards. As farm gate prices in both situations – liberalised or regulated farm gate prices – generally fall far below the threshold of a LIRP, in either case mechanisms need to be developed by companies to ensure a LIRP is reaching farmers.

**Flexible premiums**

The 2017 Cocoa Barometer consultation paper on Raising Farm Gate Prices already called for the implementation of "flexible premiums", to top up the difference between current farm gate prices and the necessary level to reach a living income. Both in regulated and liberalised origin countries, calculations should be made – at least on an annual basis – to determine what the level of the flexible premium should be to bridge the living income gap for farmers. This calculation should be based on the system described above.

In the cocoa sector, some companies are already using a variation of a flexible premium leading to a LIRP, including Tony Chocolonely's "Tony's Open Chain" model, the Fairtrade Living Income Reference Price, as well as the models of Oxfam Belgium's "Bite to Fight", and Colruyt.

**Realistic variables**

Any LIRP should be calculated on the basis of realistic current agronomic variables. This means that it needs to be guided by realistic costs of sustainable cocoa production[15], current actual yields, available labour and labour costs[16], and actual

14 The Cocoa Barometer made a comparison between various Living Income Reference Prices in 2020. According to our calculations, a credible living income reference price would be $3,166 per tonne in Côte d'Ivoire and $3,116 in Ghana. During interviews for this paper with farmer-based organisations in Côte d'Ivoire in October 2023, several farmers came up with a calculation of around $3,200 per metric tonne. These numbers are directional, companies could have different outcomes, but this would need to be coupled with a very transparent calculation method, criteria for which are set forward in this paper.

15 Including the costs of compliance to sustainability requirements, both mandatory (i.e. EUDR, national legislation, etc.) as well as the costs of compliance to sustainability programmes.

16 Though consensus is starting to form around some variables – average current yields, household size, farm size, other income streams – on other key variables there are still too many unknowns, especially around labour costs and other costs of production. The currently available data suggest it would take about 130-150 labour days, and ca 250kg fertiliser per hectare to achieve a yield of 550 kg. At present, current yields are realistic between 450-550 kg per hectare average. These data are based on a Practitioners Workshop, organised by the VOICE Network and Südwind Institut in February of 2023. This two-day workshop was aimed at identifying key variables around farm income and labour costs and was attended by a wide range of data experts. First steps are being undertaken to synthesise the vast amount of data currently being held by industry players, but the information needed for defining these variables is still too often kept out of the public domain.

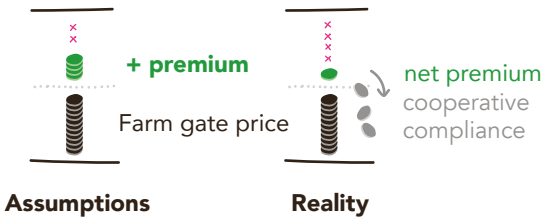
farm sizes, instead of ambitions of yields to be achieved in the future. Furthermore, LIRP calculations need to account for realistic production costs (including labour[17] and inputs) needed to achieve the stated yield rates.[18]

**Outliers vs median farmers**

Many of the calculations on approaches to increase farmer income are based on best case examples of cocoa farming, often with an ideal combination of farm size, yield, and household composition, with access to extension services and infrastructure. The result is that approaches are often only realistic solutions for a small percentage of the cocoa farmers in a company's supply chain. A LIRP – and other interventions – needs to be based on the median farmer in a supply chain and should be designed to help the majority of farmers in a company's supply chain achieve a living income, not a small selection of best-performing households in ideal circumstances.

**Sustainability premiums**

The flexible living income premiums described above differ considerably from the current sustainability premium systems, which are generally a black box that claim to do more than they can[19], regardless of whether they are run by certification systems or within company sustainability programmes. Furthermore, sustainability premium systems are not calculated on the basis of household needs; instead, they are based on what a company or a certification system feels they can afford while maintaining their market share. Additionally, most premiums are currently paid at either the cooperative or community level, and so only partly reach the farm gate. Finally, many premiums that are currently in place largely serve to cover the costs of compliance for various sustainability programmes, such as a certification or a company programme.[20]




Sustainability premiums can only count to bridge the living income gap to the extent that costs of compliance and operating costs for the cooperative are already deducted.[21] Any sustainability premium that is claiming to improve farmer income

17 Hired labour should be calculated at living wage levels, otherwise smallholder poverty alleviation strategies would be based on exploitative hired labour. The 2022 Südwind Institut "Poverty Trap" paper provides a detailed analysis why labour costs are so important and are insufficiently (if at all) taken into consideration in current poverty alleviation approaches.

18 It is important to note that most LIRP systems in place, including those of Fairtrade and the Tony's Open Chain system of Tony's Chocolonely, currently are based on desired yields of 800 kg per hectare. As we argue in the 2022 Cocoa Barometer (on pages 22-23) data suggests that beyond ca 550-650 kg per hectare any income effects of further yield increase are countered by increased costs of production.

19 Premiums simply aren't high enough premium paid to cover costs of compliance to the farmer, pay for the running costs of the cooperative, as well as create a significant net income boost to farmers.

20 For the development of this paper, consultation workshops were held with civil society and farm-based organisations in Côte d'Ivoire and in Ghana. Cooperatives indicated that the costs of running the cooperative can be around $150 to $200 per tonne. This leaves very little of the premium for distribution to farmers.

21 Please note that this paper does not argue against premiums at cooperative or community level; these are vital income streams for the functioning of cooperatives. In fact, in some standards, community pay-

must demonstrate how it reaches the farm gate[22]. Any premium that claims to reduce the living income gap can only count to the amount that goes above the amount necessary for covering compliance costs for sustainability programmes – including the additional costs for productivity increase or adoption of nature-friendly production practices, such as labour costs, input costs, etc.

### Transparency of premiums

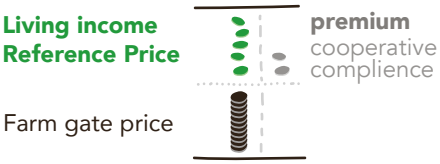
To that purpose, we recommend that premiums be split into three separate components; a part dedicated to the cooperative (based on realistic costs of running a cooperative); a second part dedicated to cost of compliance (based on realistic costs of compliance); and a third part, a living income premium that tops the current price up to a LIRP.

### Gender

If a LIRP intervention is not designed through a gender lens, there is a real risk that it will contribute to further gender inequality, by empowering male farmers only. Gender interventions must also differentiate between wives of male heads of households and households with a female head. Interventions for the former could include ensuring part of the payment goes to the women, that women also have access to training, etc. For the latter, this could also ensure land tenure security measures, access to market drives, and more.

### Living income reference price system

Concretely, all companies must commit to a time-bound, gender-sensitive, action plan to bridge the living income gap, which includes the implementation of a living income reference price system. This living income reference price system must be based on realistic averages and must provide a clear breakdown between that part of the premium that goes to cover the farmer's living income gap, and those parts that cover compliance costs and running of the cooperatives.




## Non-purchasing interventions

Beyond pricing, it is possible for non-purchasing interventions to reduce the living income gap. Such interventions could include activities aimed at increasing access or reducing costs, such as reducing post-harvest losses, increasing access to education and healthcare, etc. Collective efforts (such as village savings and loans associations), as well as interventions such as cash transfers, can further reduce the living income gap.

ments and community decision making on how premiums are spent are mandatory, and often rightly so. This paper argues that in addition to collective premiums, care needs to be taken that these premiums are not double counted: they cannot be spent collectively and at the same time count as individual income.

22 In fact, while much of the debate about the merits of traceability has been focusing on tracing cocoa volumes from farm to traders and further downstream, tracing premium payments in the opposite direction (i.e. up the supply chain from traders to coops to farm gate) is equally of critical importance to reforming the cocoa sector.

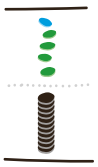
Considering the current reality of cocoa farming, there still is an almost certainty that the living income gap will not be closed by these interventions alone. Though additional interventions can be valuable extra components to a company's purchasing practices and reduce the living income gap, they cannot be a substitute for what is the core of the issue: a remunerative price at farm gate level that bridges the remaining income gap.[23]

### Cash transfers

Cash transfers can provide a valuable means to decouple – at least in part – poverty interventions from a purely market-based approach.[24] This is necessary because poverty is measured in people per household, not in the tonnage of production. Furthermore, especially for those segments of cocoa farmers that grow less cocoa or have a weaker economic position – such as households with smaller plots, more dependents, and/or female-headed households – interventions are needed that are not just based on volumes of cocoa sold. As such, not all poverty can be tackled through a market dynamic. If companies can prove that cash transfers add to the net income of a cocoa household – or reduce their costs – the added net income and/or reduced costs can be subtracted from the living income gap. Cash transfers have proven to work well in many agricultural and non-agricultural programmes throughout the world. However, they are tools to reduce the living income gap, not to bridge it completely. Even when cash transfer programmes are successful at scale, companies will still need to review their pricing as part of a purchasing practices strategy.[25]

### Payment for environmental services

Another way that farmers can receive a higher farm gate remuneration is through payments for environmental services (PES), such as reforestation and forest protection programmes, reducing the use of harmful agrochemicals, and encouraging biodiversity conservation. If PES are to make a meaningful contribution to reducing the living income gap, then these schemes must ensure the payments are high enough to bear the cost of compliance and loss of earnings incurred by implementing actions the environmental services.



Interventions: PES, Cash transfers, etc

**Living income Reference Premium**

Farm gate price

## Additional interventions

Though it is clear that purchasing practices of companies must include a living income reference price model, this will not solve all of the problems. In fact, approaching farmer poverty through purchasing practices brings in several unresolved issues that will require further thought and additional interventions.

23 Increasingly, industry is saying that there needs to be a smart mix of interventions in order to bridge the income gap; this implies that pricing must be part of the mix.

24 Such as Nestlé's Income Accelerator programme.

25 In specific circumstances where cash transfers are sufficient to bridge the living income gap, there still remains the requirement to companies to transparently communicate how this is achieved. In essence, the living income reference price systems still remains valid, with the additiona premium per tonne being zero.

**Averages vs segmentation**

A LIRP enables an average household to earn a living income. However, many farming households will require additional interventions to bridge the income gap, such as gender-specific interventions, land tenure security, financial literacy education, access to credit, and other structural changes. Beyond averages, farmer segmentation can help to design additional interventions based on specific types of household needs. Cash transfers can be useful interventions to help more vulnerable segments, as these are generally not based on the tonnages of cocoa produced. The fact that a LIRP helps well-performing farmers more than the poorer-performing farmers is increasingly used as an argument not to pay a LIRP. This position is only tenable if the aim is to keep every farmer at the edge of poverty, rather than allowing outliers to become affluent.

**Gender**

Segmentation becomes especially relevant when it comes to gender equality. Female-headed households are strongly overrepresented in more vulnerable segments of cocoa growers. In addition to higher prices, a gender lens is needed. This can include literacy and numeracy programmes for both adult females and girls, land tenure security for female-headed households, access to training and markets for women, and many more.

**Traders, brands, and retailers**

Though all companies should incorporate the payment of a living income reference price at farm gate, not all companies have direct relationships with all the farmers supplying to them, either directly or through cooperatives. Traders tend to have more direct relationships with farmer cooperatives and play a pivotal role as enablers towards both ends of the supply chain. Traders usually have long-term contracts with brands, yet they do not pass this long-term on to the cooperatives. Every cocoa trader should have a published living income reference price per cocoa sourcing region and should have time-bound action plans in place to ensure this price is delivered at farm gate level.

At the same time, brands and retailers tend to put price pressure further upstream.[26] Therefore, both brands and retailers should equally have in place a public policy that requires the payment of a living income reference price. This requirement must be coupled with a clear commitment to paying for this service to their upstream suppliers. Too often, brands tend to point towards the traders to solve the problem, whilst simultaneously trying to undercut their suppliers.

**Scale**

Although living income reference prices are starting to be rolled out increasingly in the cocoa sector, the tonnage of cocoa sourced with the use of these principles is still marginal compared to the size of the global cocoa production. However, the principles are applicable regardless of the size of the cocoa or chocolate company. Collaborative sector-wide efforts could likely increase the speed and scale of potential uptake. Additionally, flanking policies – such as rural development frameworks, supply management policies, income diversification projects, etc. – will be required to combat potential deforestation and waterbed effects towards other commodities.

26 The fact that downstream actors such as brands and retailers are always kicking the cost of compliance can up the supply chain towards the traders should show that it is actually in the industry's interest to require good purchasing practices as part of a mandatory regulatory requirement.

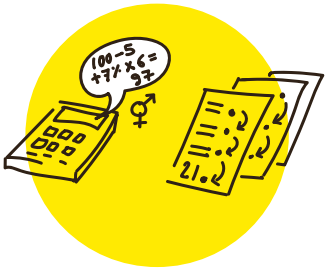
**Enabling environment**
Though companies don't need to wait for the necessary enabling environment to start acting on the requirements above, an enabling environment would speed up action, and create the necessary level playing field to counteract free riders. To that purpose, these purchasing practices should be enshrined in regulations in major consumer countries. Verifiable transparency systems on both products and finances would be extremely helpful, as would systems to contract directly with cooperatives. Verifiable transparency systems for finances would require the ability to trace payments made not just to the cooperative level but to the farm gate level.

## Summary

The core of any good purchasing practices is a farm gate living income reference price (LIRP). Companies must commit to a time-bound, gender-sensitive, action plan to bridge the living income gap, which includes the implementation of a living income reference price system. This must be based on realistic averages and must provide a clear breakdown between that part of the premium that goes to cover the farmer's living income gap, and those parts that cover compliance costs and running of the cooperatives. Beyond pricing, it is possible for non-purchasing interventions to reduce the living income gap, such as cash transfers and payments for environmental services, but they cannot be a substitute for a LIRP.

## Primary asks of companies

**Living Income Reference Price**
Retailers and brands must commit to requiring a publicly available LIRP from the traders they source from and must be willing to pay for this. Traders must commit to paying a publicly available LIRP. This commitment must include transparent calculations of how the farm gate price they pay is sufficient to close the remaining gap and must be applicable to the majority of the cocoa farmers in the supply chain, not just some outliers.



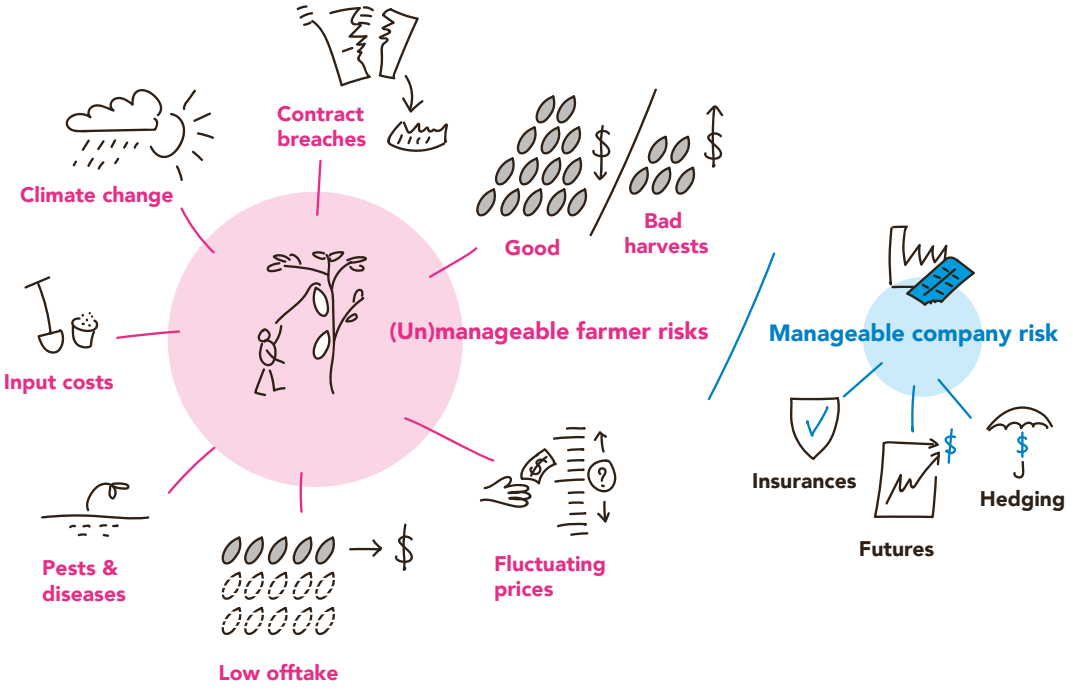
**Transparent calculation**
Every company – retailer, brand, trader – should have a calculation of the living income gap of median farmers in their supply chain, and a timebound gender-sensitive commitment to close this gap.

**Review**
All actors need to regularly review their income approaches with a gender lens to ensure interventions actively combat gender inequality, rather than exacerbate it.

## Secondary asks of companies

Income effects of non-purchasing-based interventions (such as community investments, cash transfers, and payments for environmental service) must be communicated transparently and based on the net income gender-sensitive effect on the farmer, not on the cost to the company.

Premiums should be transparently broken down into three distinct components: cost of compliance, cooperative operation and governance costs, and net additional income for farmers.




# Acceptable risk

Although price is a key element of purchasing practices, it is by no means the only aspect. Good purchasing practices also require redressing the unequal distribution of risks. At present farmers bear practically all the risks, but do not reap the rewards. In cocoa, the weakest shoulders bear the heaviest burdens. These risks include uncertainty of volume and price of sales, uncertainty of input costs, vulnerability in the face of stronger buyers, pests and diseases, climate change, as well as the volatility of market prices and weather, which has significant impact on this agricultural crop. Furthermore, farmers often have to deal with unclear and complex contracts (in terms of tonnage, price, timing of delivery), contracts that moreover are often not respected. Long-term asymmetric contracts coupled with standardised contracts and accessible grievance mechanisms are key elements in reducing the risk for farmers.

**Standard contracts**

A first simple step in reducing risk and creating clarity and assurance for farmers is the adoption of standard contracts at cooperative/farmer level. A wide range of different contracts are the cause of confusion and exploitation towards farmers.[27] A standard contract would solve a lot of difficulties here already, where farmers or cooperatives would only have to ensure that the key variables are filled in properly (such as volumes, expected quality, price, payment terms, delivery date). Especially in regions with lower literacy and numeracy rates, standardised contracts provide significant improvements. Though this is not the key ask of this paper, it would be a

27 One example provided at a consultation workshop for this paper in October 2023 was the fact that a missing signature on page 12 of a contract was used as a reason to reduce the premiums. Though this is anecdotal, examples of this were rife during conversations the authors of this paper held with farmer organisations in West Africa.

fast and easy win for all parties involved. The cocoa sector is very used to working with standard contracts, as further downstream virtually the whole trade is based on standardised contracts that are formulated by the Federation of Cocoa Commerce (FCC). There is no reason not to continue this to farmer level.[28]

## The case for long-term contracts

Chocolate brands generally know how much cocoa they will need on a year-to-year basis – their forecasting departments tend to have a pretty clear understanding of how much cocoa they will need several years in advance. Often, chocolate brands already have long-term contracts with the traders that supply them. These traders, however, do not have similar contracts with cooperatives and farmer organisations. Brands should require the same length of contracts to be provided to the cooperatives that supply their traders. In return, traders should require brands to engage in risk sharing. When contracts are long-term and trust is built, it provides assurance on consistency of volumes for the buyers and comfort of income flow for the farmers. In effect, long-term contracts could contribute to a better function of the market in the long-term.

### Benefits to farmers

Long-term contracts[29] provide key benefits to buyers and producers, including lower total transactional costs and improved profitability. They would allow farmers and cooperatives to invest in their infrastructures, farms, and sustainable practices, and could play a key role in driving more sustainable agriculture[30], particularly in the face of climate change and more resilient food systems. They would also open the possibility of spreading payments throughout the year – as prepayments, not as delayed payments – creating a healthier cashflow situation for households.

### Benefits to companies

This is not just a risk-sharing effort. It will also be beneficial to the buyer: long-term contracts ensure security and quality of supply and also enhance traceability and transparency. Long-term contracts often have a built-in mechanism for addressing multi-year issues like sustainability goals.[31] Furthermore, long-term, transparent MOUs and higher prices are rewarded by farmer cooperative with stronger buyer loyalty over many years. As a brand's sustainability goals get more ambitious and impactful, achieving them will likely become more difficult, and new tools will be required. Long-term contracts can be a key tool for buyers and producer groups to drive change and set specific dates for completion.

## Asymmetrical contracts

Being tied to a single buyer can be a double-edged sword for farmers and farmer cooperatives as it can create dependencies and prevent them from taking advantage of higher prices elsewhere. There is a clear power imbalance between the various actors in the chain. In the current system most risks (on volume, price, delivery) are

---

28 Or at the very least to cooperative, farmer organisation, and/or purchasing clerk level.

29 The name of such an agreement can differ per country. In Ghana, contracts are with the CMC/Cocobod, and supplier agreements are signed with traders. In that context, one would speak of long-term supplier agreements.

30 Long-term contracts could also potentially help to reduce incentives for overproduction, as farmers/co-operatives with a contract for a fixed amount of cocoa paid at reference price would have less incentive to grow more if extra production would only be sold at much lower prices. This hypothesis needs further validation and research, however.

31 How Long-Term Contracts Can Help Drive More Sustainable Agriculture, Jason Clay, Dec 2018

covered for the buyer, but farmers find themselves often waiting for a selling contract resulting in them accepting hunger prices. This means that long-term contracts need to be asymmetrical in nature, providing farmers more rights, while putting more responsibilities on the shoulders of the purchasing companies.

Concretely, an asymmetric contract needs to commit buyers to buy a minimum tonnage of cocoa at an agreed-on price, but the farmer needs to be free to sell to a different buyer if they can get better conditions.[32] Price renegotiation clauses should be part of such long-term asymmetric contracts, to allow farmers to take into account fluctuations of the prices of raw materials and cost of living.

### Minimum requirements

Long-term asymmetrical contracts should cover some key elements, including a specific timeframe (3 years or more), (realistic) minimum volumes, the living income reference price, as well as a renegotiation mechanism in case of unexpected events like a global pandemic, cost of living crisis, or crop failure due to pests or weather. Quality premiums, certification premiums, and any other relevant payments should be clearly distinguished within these contracts. They should also include mutually expected/required sustainability and governance efforts as well as payment terms that ensure a healthy cash flow for the farmer. Additionally, they may include further benefits like access to services (schooling, healthcare, contributions to pension schemes) and banking products.

## Enabling environment

### Respect the contract

At present, there is a big discrepancy between what traders announce (or put in draft contracts) to cooperatives (total volume and share of certified), and what is really bought at the end of the harvest (at which point the contract is formalized or updated with final real figures). Contracts are often not respected, or the unclarity of contracts is abused. As a result, many cooperatives are left with volumes to sell on the "informal" market, or with certified cocoa that has to be sold at the bulk price, resulting in lower prices. To avoid these malpractices of market power, penalties should be included in contracts for traders not respecting their commitments and contracts. Companies should have effective, accessible complaint mechanisms in line with the UN Guiding Principles that allow farmers to raise & resolve such issues at a higher level within the company and with external arbitrators. These mechanisms should be transparent and accessible to farmers.

### Organised vs. unorganised farmers

Long-term asymmetrical contracts – as well as credible and transparent LIRP payments – will require long-term, functioning farmer organisation structures. Indeed, there is a wide spectrum of quality of farmer cooperatives, some of which are more democratically run than others, and some of which have real problems with corruption and finances not finding their way to the members. There is also a large difference between self-organised farmers and trade-organised farmers such as those in the Licensed Buying Company model in Ghana. More than a few cooperatives operate more as shell companies for cocoa extraction by traders than as organisations that are operating in the best interest of their members.



32 This should be a first right of refusal contract, not a first right to offer, as the latter would still make the farmer vulnerable to refusal of contracts.

In that light, it is of importance to increase the amount and quality of bottom-up initiatives of self-organised and democratically organised farmer organisations.[33] There is probably a minimum size of the cooperative (either in members or in tonnage) to be able to provide efficiency of scale or buying/selling power. Part of a solution to the challenge for farmers and farmer organisations could be that companies make supplier commitments to communities, and those communities then choose one or more cooperatives through which they want to commercialize. To this end, company codes of conduct should explicitly recognise the right of farmers to organise collectively. More discussion on this topic is needed going forward.

**Size of companies**

For effective risk mitigation, it may be necessary to define different buyer categories: when a small buyer embarks on a multiyear contract, their business may collapse when consumer demand drops, while they still must buy cocoa. However, large multinational companies and traders are in a different ballpark. Over the past decade, the tonnages of the large brands and traders have remained quite stable. It should be possible to oblige large companies to embark on multi-year contracts for a large percentage of their current purchasing volume, for example, to set 70% of their bean purchases in long-term contracts for the next 3 years. Ironically, it's often small companies who do more risk-sharing with farmers. It should be the opposite! The larger the company, the more the company should be willing to reduce or mitigate the risks for farmers.

**Supply management**

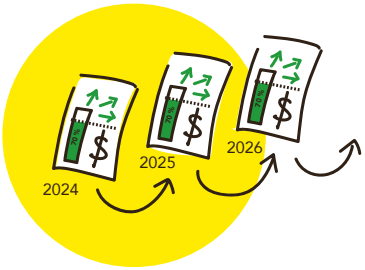
Long-term contracts and living income reference pricing don't solve all problems, and solutions will need to be found for what to do with the surplus production in bumper years. It could be argued that the key to that problem lies in rural development policies and supply management, both of which are largely the remit of government actors, not of the private sector.

33 Throughout the world and throughout history, one of the clearest guarantees for improvement of sales criteria has been for farmers to self-organise. This is clearly also the case for cocoa, although this falls outside the scope of the present paper.

## Summary

Although price is a key element of purchasing practices, it is by no means the only aspect. Good purchasing practices also require redressing the unequal distribution of risks. Long-term asymmetric contracts coupled with standardised contracts and accessible grievance mechanisms are key elements in reducing the risk for farmers.

## Primary asks of companies




**Asymetric long-term contracts**
Traders should implement long-term asymmetrical contracts with farmer organisations, within a specific timeframe, including realistic volumes, the living income reference price, renegotiation mechanisms, and clear rights and responsibilities for buyers and farmers.

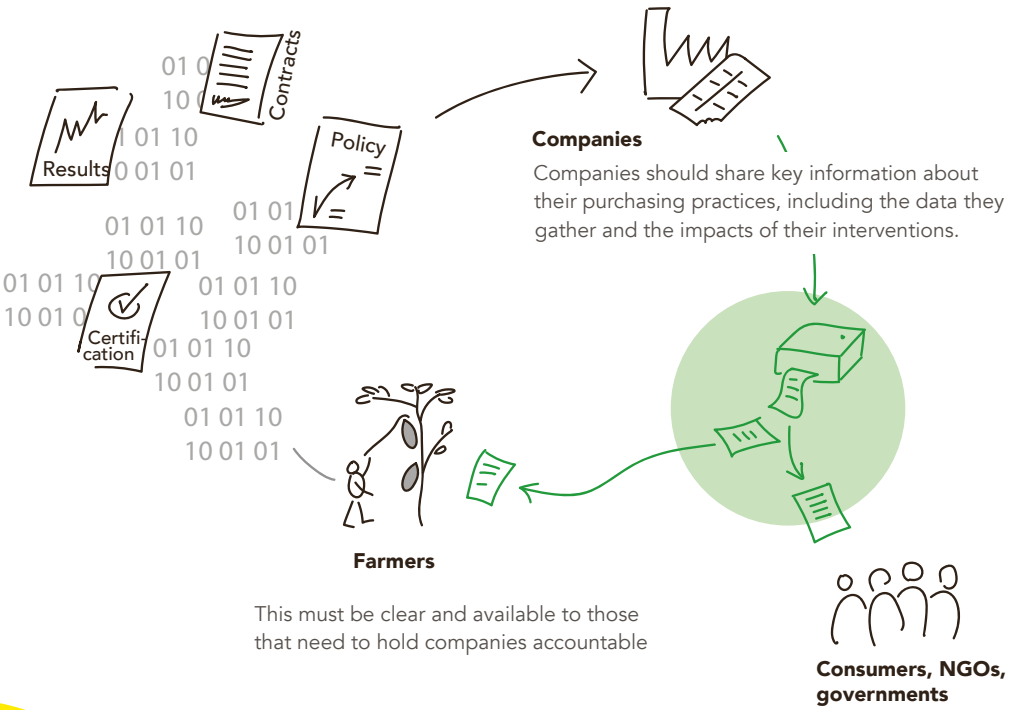
Retailers and brands should require long-term asymmetrical contracts of traders, whilst being willing to pay for compliance to the contracts.

**Respect the contract**
Contracts and volumes must be respected, and effective complaint mechanisms with real consequences for noncompliance should be in place.

## Secondary asks of companies

Standard, sector-wide contracts for trading at farmer/cooperative level should be implemented, that provides clarity and assurance to farmers and farmer organisations.

The development of strong and democratically run cooperatives should be supported as a key mechanism to reduce risks for farmers.




# Transparency & accountability

Credible living income approaches that include effective purchasing practices are not just a moral imperative; with the advent of Human Rights and Environmental Due Diligence regulations at European and national levels, they will become part of a business and legal imperative. It will become increasingly important for companies to be able to communicate credibly and transparently about their purchasing practices, both to ensure accountability as well as to ensure farmers properly understand their rights and obligations. Furthermore, in order to properly address purchasing practices over the medium to long-term, they will have to become part of a level playing field, meaning they will have to be explicitly stipulated in regulation.

Transparency and accountability should also lead to a cycle of continuous improvement in purchasing practices. There are several elements that will aid transparency and in turn, increase accountability on purchasing practices.

### Living income policy

The first prerequisite is that every company should publish a time-bound living income plan[34] that explicitly includes purchasing practices as a key component in ensuring sustainable cocoa. All strategies and action plans that are detailed in this, such as pricing and risk-sharing strategies, need to be supported with calculations and transparency about the variables that inform those calculations.

### Responsible purchasing KPI monitoring

As part of this living income plan, companies should have internal responsible purchasing KPIs that are directly linked to their sustainability goals, and that are



34 A good example of such a living income policy is that of Chocolat Halba.

linked to their financial incentive systems. These KPIs should be annually reported on, as well as progress in closing LI gaps – disaggregated by gender. Progress should not only be assessed on how many farmers are earning a LI but also what the relative income improvements have been made, to avoid the risk that companies simply consolidate their supply chains and only source from better off farmers. This problem will not be solved by simply kicking the poor and the weak out of the cocoa supply chain.

**Indirect sourcing**
Indirect sourcing is incompatible with sustainability. Either a company knows where it is sourcing from, and therefore knows which challenges it is facing and which solutions are needed to bring to the table, or it doesn't. As such, there is no place for indirect sourcing in good purchasing practices. National traceability systems can play an important role in this. However, they have been promised for many years, and still not delivered. There is hope that the upcoming EUDR regulation will speed up the process of this development.

**Data transparency**
Transparency on aggregated agronomic data such as average yields, farm size, costs of production and required labour should become standard practice. This data is key to designing targeted support for the most vulnerable farmers, including women, and reducing gaps in income, connectivity, and market access. This transparency is also expected on all sustainability initiatives that can help to understand what works well or not, and where, to avoid inefficiencies and ensure under-addressed regions can also be targeted.

**Data ownership**
The cost and burden of data collection and disclosure should not be borne by farming households. As such, farmers should be rewarded for sharing data – coupled with contractual assurances that sharing data does not lead to disengagement. If done well, these processes can facilitate strong feedback loops between farmers and companies. Rather than being treated as data providers and forced to comply with unilateral requirements from purchase agreements, farmers can be mutually beneficial partners to other supply chain actors, provided the correct incentives are in place. At present, farmers are often mapped several times every few years by different companies – and required to help in the process[35] – while still not owning their data. This is both inefficient and unethical. Farmers and farmer organizations should be remunerated adequately to capture and manage data from their members so that they can own it[36] and use it to facilitate feedback not only with companies but their members as well.

**Contract details**
Together with the introduction of standard contracts, it should be possible to publish data, at the very least at an aggregated level, on contract length, price guarantees, premiums to be paid and penalties for non-compliance. This should be broken down into farm gate price, quality premiums, certification premiums, and any other relevant differentials. This should also be coupled with transparency on the costs side; certifications costs borne by the traders and what is deduced from the cooperatives' payments.



35 Sometimes even being required to house and feed the staff of the mapping companies for lengthy periods of time, or even purchase the equipment required.

36 Farmers could, for example, refuse cooperation if there is no ownership of data.

**Payment recording**
Verifiable payments are an important part of increasing transparency. Companies should make available the traceability of the invoices, the points of purchase, the buyers (cooperatives or individual buyers), the place of purchase, and the plantation of origin of the purchased product. Other elements that could be helpful are keeping a record of the follow-up of the annual purchase invoices and keeping an up-to-date list of the approved and non-approved buyers. These verifiable payments could also help farmers and cooperatives comply with EU traceability requirements as defined in the newly adopted EU Deforestation Regulation.[37]

**Digital payments**
Stimulating measures to include farmers in the digital money system will aid traceability and transparency, and lower fraud, violence, and exploitation. It also brings farmers out of the ranks of the unbanked, so they can more easily access lines of credit etc. This must be done sensitively and consultatively so that it never penalizes the farmer but is a net win for them. The costs of digital transactions should be in addition to and not deducted from the income of farmers. This could also be designed in such a way as to allow farmers to hold cooperatives accountable.

**Sector-wide reporting**
Ideally, there would be a sector-wide consensus on reporting formats on purchasing practices, to ease comparability and facilitate areas of collaboration. Attempts for this have been made – generally at a less-than-ambitious scale – in the textile sectors regarding a living wage.[38] Care should be taken that competition law is complied with, but within for example the various national Initiatives for Sustainable Cocoa (ISCO) commitments there should be space for more transparent, accountable, and comparable reporting.

37 A best-in-class example of farm gate pricing transparency can be found in fine flavour cocoa trading company Uncommon Cacao, who for many years already have been publicly disclosing farm gate pricing on all their cocoa purchases in their annual Transparency Report. Though this would require a different scale for bulk cocoa traders, the principle remains the same.

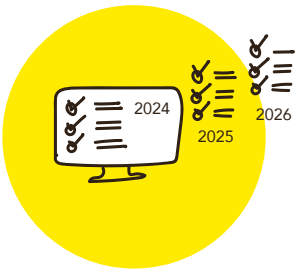
38 Including the Common Framework for Responsible Purchasing Practices, the ACT on Living Wage, and the self-assessment of the textile sector facilitated by the IMVO Convenant in the Netherlands.

## Summary

It will become increasingly important for companies to be able to communicate credibly and transparently about their purchasing practices, both to ensure accountability as well as to ensure farmers properly understand their rights and obligations. Transparency and accountability should also lead to a cycle of continuous improvement in purchasing practices. Companies should develop a time-bound living income policy, and annual publicly report on responsible purchasing practices KPIs.

## Primary asks of companies

**Publish a time-bound policy**
Companies should publish a time-bound living income policy, and annually report on how the living income gap is closed, including a gender-disaggregated measurement




**Report**
Companies should publicly report annually on responsible purchasing KPIs, including on volumes and farm gate prices paid.

## Secondary asks of companies

Farmers should be paid for their data sharing and ensure they have access and ownership.

# Conclusion

The daily reality for the vast majority of cocoa farmers is (extreme) poverty. In addition to changes in governance policies, and in order to provide a business case for improved agricultural practices, companies must change their purchasing practices. This is not dependent on sector-wide collective action but can be implemented by individual companies almost directly.

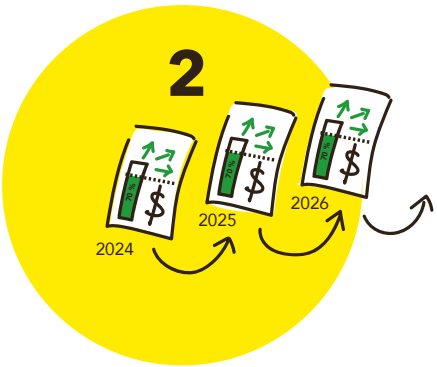
Current business practices largely focus on agronomic approaches and will not suffice to reach a living income. Though there is a role for governments in dealing with these issues, that is not an excuse for companies to not do what they can. This paper focusses on what companies can do better in their core business; the buying of cocoa.

The core of any good purchasing practices is a farm gate living income reference price (LIRP). Companies must commit to a time-bound, gender-sensitive, action plan to bridge the living income gap, which includes the implementation of a living income reference price system. This must be based on realistic averages and must provide a clear breakdown between that part of the premium that goes to cover the farmer's living income gap, and those parts that cover compliance costs and running of the cooperatives. Beyond pricing, it is possible for non-purchasing interventions to reduce the living income gap, such as cash transfers and payments for environmental services, but they cannot be a substitute for a LIRP.

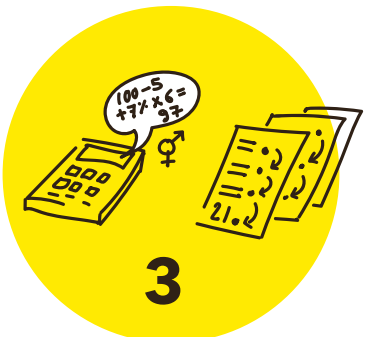
Although price is a key element of purchasing practices, it is by no means the only aspect. Good purchasing practices also require redressing the unequal distribution of risks. Long-term asymmetric contracts coupled with standardised contracts and accessible grievance mechanisms are key elements in reducing the risk for farmers.

It will become increasingly important for companies to be able to communicate credibly and transparently about their purchasing practices, both to ensure accountability as well as to ensure farmers properly understand their rights and obligations. Transparency and accountability should also lead to a cycle of continuous improvement in purchasing practices. Companies should develop a time-bound living income policy, and annual publicly report on responsible purchasing practices KPIs.

**Pay a fair price**




**Share the risks**




**Be accountable**

## Colophon

Text: Antonie C. Fountain, VOICE Network
Additional contributions: the text of this draft of the consultation paper is the result of several rounds of consultation with the Cocoa Barometer Consortium members and other stakeholders in the cocoa sector.
Design: Roelant Meijer (Tegenwind.eu)

Citation: Fountain, A.C. (2023): Good Purchasing Practices in Cocoa, a Barometer Consultation Paper

Published by: the Cocoa Barometer Consortium

Administered by: the VOICE Network

The Cocoa Barometer Consortium consists of: ABVV/Horval, Action against Child Exploitation (ACE), Alisos, Be Slavery Free, EcoCare, European Federation of Food, Agriculture and Tourism Trade Unions (EFFAT), Fern, Freedom United, Global Labor Justice/International Labor Rights Forum, Green America, IDEF, Inades Formation, INKOTA-netzwerk, Mighty Earth, Nature and Development Foundation, Oxfam America, Oxfam Belgium, Oxfam Ghana, Oxfam Novib, Public Eye, Roscidet, Rikolto, SEND Ghana, Solidaridad Europe, Solidaridad West Africa, SÜDWIND Institut, Tropenbos International, Tropenbos Ghana, WWF Belgium, WWF France.

Contact
Requests for information can be addressed to: antonie@voicenetwork.cc

Copyright
The 2022 Cocoa Barometer is available as an interactive publication online, as a digital download, and as a hardcopy printed publication. The infographics used in this document can also be downloaded separately. We encourage the use of this data in other publications, provided proper references are given. Published under Creative Commons License Attribution-ShareAlike 4.0 International

**www.voicenetwork.cc**

**Produced with the support of the Directorate-General for Belgian Development Cooperation (DGD).**
Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the Directorate-General for Belgian Development Cooperation (DGD). The DGD can not be held responsible for them.

Belgium
partner in development