
UNIT 2 MARKET MECHANISMS FOR CSR

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2.1 INTRODUCTION

CSR (Corporate Social Responsibility) refers to the balancing practice of interests between different stakeholders of a firm in managerial decisions or business operations. CSR is also considered to be an umbrella term under which the ethical rights and duties existing between companies and society are debated. Doing business with responsibility is key for the success of any business in today's world which demands ethical and sustainable value chain management. The value chain refers to all the functional inputs that a firm provides along the process of transforming raw materials to delivered products or services. The priority in this realm of CSR is increasing business opportunities and profitability, while also creating social and environmental benefits, by improving operational effectiveness throughout the value chain be it upstream in the supply chain or downstream in the distribution chain. This CSR approach, which has become increasingly popular among both academics and corporate leaders, may be considered roughly analogous to the “shared value” framework, in which the corporation seeks to co-create economic and social value.

In this unit you will read about the role of commodity standards and conditionalities on raw material production of commodities like cotton, tea, coffee, fish, palm etc. You will also learn about the dynamics of factors of production, public market mechanism and how it relates, correlates and affects CSR. After reading this unit, you will be able to

- Discuss the conditionalities on the raw material production of selected agricultural commodities
- Explain the role of Voluntary Sustainability Standards in ensuring sustainable production
- Discuss the link between market mechanism and CSR

2.2 CONDITIONALITIES ON RAW MATERIAL PRODUCTION

Most of the raw materials required to make finished goods comes from the developing countries. For raw material supply chains to be more sustainable,

it is important to ensure equitable and ethical supply terms for the producers of these raw materials. It also calls for the companies to play a positive role in improving social, ethical and environmental standards along their supply chains. It is important that the minimum requirements in doing business with them are clearly specified in their policies related to the suppliers code of conduct. Other concerns such as animal welfare, use of harmful substances in production and sustainable packaging so as to reduce the environmental and social impact of packaging should also be reflected in the company's policy. For better understanding, let us now discuss the conditionalities on the raw material production of some of the commodities.

1. Production of Cotton

Cotton is the most important raw material used in the textile industry, amounting to around 40 per cent of the raw material used. Cotton industry also provides livelihood to millions of people globally. Hence it is important that an industry of such high global impact works sustainably. The issue of sustainable cotton production needs to be discussed for the following reasons:

- i) High water consumption. The global average water footprint of cotton fabric is 10,000 litres/ Kg (Turner, 2019).
- ii) Excessive use of pesticides leads to water pollution and soil contamination. Cotton is said to cover 2.5 % of the world's cultivated land, yet it uses 16 % of world's insecticides, more than any other major crop (Turner, 2019).
- iii) Use of child labour and other issues related to workers' rights. Cotton is one of the goods most commonly produced using forced labour. Forced labour exists in nine countries producing 65% of world's cotton.
- iv) Use of genetically modified cotton. In 2016, 64% of the cotton grown was genetically modified. Farmers are unable to use the seeds of GM crops for the next season and become perennially dependent on the MNCs for seeds. Besides, the GM crops are more input intensive.

Several initiatives have been taken up to address these issues. The Better Cotton Initiative is a multistakeholder initiative which was started in 2005 to reduce the water and pesticide used in cotton production. It is a global not-for-profit organization and aims to make cotton production better for the farmers growing it, the environment in which it is grown and for the future of the cotton sector.

Better Cotton Initiative has operations with implementing partners in 21 countries including India, Pakistan, South Africa and the USA. It trains the farmers for producing sustainable cotton and then certifies them to recognize the produce as sustainable. The training encompasses seven principles including environmental factors such as crop protection, water stewardship, soil health, land and biodiversity; as well as social factors such as decent working conditions and fair compensation (Thacker, 2019).

2. Production of Tea

Tea is one of the most popular drinks next to water. There are more than 35 countries which produce tea. However, India and China combined

Alternative Trajectories in CSR produce more than 50 per cent of the global tea produced. This sector provides employment to millions of people worldwide and is a vital part of the economy of countries which export tea. Sustainable tea production is important as the sector faces several challenges in this direction. Some of them are listed below:

1. The working conditions of the people working in this sector is marred by low wages, discrimination of workers along both gender and ethnic lines and occupational hazards in terms of injuries during work and exposure to pesticides which are applied without proper protection.
2. High biodiversity areas are deforested and converted into tea plantations causing bio-diversity loss. Energy consumption in processing of tea is very high. The excessive use of pesticides in certain areas leads to water pollution and reduced soil biodiversity.
3. There is uneven value distribution along the supply chain where a major share of the price goes to the multinational tea packers and brokers involved in blending, packing and marketing.

There are several CSR initiatives that provide their services to tea packaging companies as well as well as producers. Some of these initiatives include Ethical Tea Partnership (ETP), Rainforest Alliance (RA), Fair trade (FLO) and Organic (IFOAM). ETP, aims to improve the social conditions within the existing supply chains of mainstream market players. Fairtrade, on the other hand, has been specifically set up to address disadvantaged producers and workers by setting up alternative trade chains. IFOAM focuses primarily on environmental aspects and organic farming, while Rainforest Alliance covers both social and environmental aspects.

3. Production of Coffee

Coffee cultivation has drawn widespread attention in the past few decades for its role in supporting biodiversity. Sustainable production of coffee has both environmental and social issues. Traditional coffee cultivation is done under moderate to dense shade of native forest trees. This practice allows the biological diversity of the region to flourish amidst coffee plantation. Such coffee plantations provide habitation to migratory birds, attracts pollinators like bees, stabilizes soil during heavy rains, replenishes soil nutrients and stores carbon. However, with agricultural intensification, coffee growers have started growing coffee bushes closer to each other and without any shade which has an adverse impact on biodiversity of coffee growing regions. The demand for more chemical fertilizers and pesticides becomes much higher in a monoculture sun-grown coffee plantation than for the polyculture shade-grown. Per hectare use of pesticides and insecticides in coffee production is ranked as number three in the world (Persson, 2008).

Besides the environmental concerns to sustainable coffee production there are also some social concerns as well. Around 70 per cent of the world coffee is produced on farms smaller than 10 hectares. A majority of these are small family farms ranging between 1 to 5 hectares. Between 1962 and 1989 the world's coffee market was regulated by the International Coffee Agreement (ICA) and was signed by most producing and consuming countries. The prices were regulated and the quota fixed for each producing country. Later

the quota system was abolished as it prevented free trade and the coffee market is no longer regulated by ICA. Since then, one of the causes of concern in this sector has been overproduction and decline in prices. This in turn has resulted in lack of food supplies, reduced education of children and debt trap among coffee growers.

The Common Code for the Coffee Community

The Common Code for the Coffee Community, 4C, is a joint project between different stakeholders in the coffee market to achieve greater sustainability and responsibility in the coffee sector (Persson, 2008). The 4C code of conduct applies to any producing entity in any coffee producing country which wishes to sell coffee as 4C Compliant. The main aim of 4C is to reach out to the coffee producers and to bring them into compliance with a basic level of sustainability and raise the social, economic and environmental conditions of coffee production and processing across the globe.

In order to achieve this, the code of conduct comprises of 27 principles across the social, economic and environmental dimensions and 10 unacceptable practices which have to be excluded before applying for the 4C verification.

The unacceptable practices cited include

- Worst forms of child labor.
- Bonded and forced labour
- Trafficking of persons
- Prohibiting membership of or representation by a trade union
- Forced eviction without adequate compensation
- Failure to provide adequate housing where required by workers
- Failure to provide potable water to all workers
- Cutting of primary forest or destruction of other forms of natural resources that are designated by national and/or international legislation (protected areas).
- Use of pesticides banned under the Stockholm convention on Persistent Organic Pollutants, POPs, and listed in the Rotterdam Convention on Prior Informed Consent.
- Immoral transactions in business relations according to international covenants, national law and practices (May be included in rules of participation later on – still under discussion.). (Common Code for the Coffee Community Association, 2004, pp. 12-13)

4. Seafood Production

Since the 1990s, the private sector has made conscious efforts to improve the sustainability of seafood production practices. Using market based tools such as consumer awareness campaigns, buyer engagement and certification schemes, the sustainable seafood movement aims to (a) educate consumers so they can make more informed seafood purchasing decisions and (b) incentivize seafood supply chains to improve the environmental and social aspects of production practices (Packer et. al., 2019).

Alternative Trajectories in CSR Some of the sustainability concerns in the seafood markets include:

1. Environment: Issues related to greenhouse gas emission, energy use, waste, pollution and water use in fishing and processing activities
2. Human Rights and Labour Practices: Working agreements, working conditions, health and safety, fair wages, human rights
3. Community engagement: resolving resource use conflicts with local communities, providing employment to the locals, investing in local facilities, and improving the lives of community surrounding company operations.
4. Sustainable fisheries: aspects related to scientific fisheries and ecosystem impacts

Activity 1

Visit a Company which uses any of the above commodities as raw materials and has to deal with their procurement. Discuss with them and write about how they ensure equitable and ethical supply terms for the producers of these raw materials.

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Check Your Progress - 1

- Notes:** a) Write your answers in about 50 words.
b) Check your answer with possible answers given at the end of the unit.

1. Write about any two issues in sustainable cotton production.

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2. Write about two sustainability concerns in the seafood market.

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2.3 ROLE OF VOLUNTARY SUSTAINABLE STANDARDS

The corporate sector across the global faces varied public-driven regulations of doing business, which has been reduced over time to facilitate business organizations. The public policies are increasingly providing legal ground for safety and quality standards with accurate information about the characteristics of products, which are meant to protect consumer rights. Quality certification programmes help consumers identify high quality products or sellers in markets with information asymmetries.

Mandatory standards are standards that have been incorporated into a government law and require compliance by law, regulation, government statute policy, or contractual agreement. Failure to comply with a mandatory standard usually results in sanctions such as civil or criminal penalties. There are thousands of voluntary standards addressing almost every type of consumer product on the market. These voluntary standards are considered industry best practices or “industry consensus” standards. Increased use of voluntary programmes in businesses as an alternative to mandatory approaches raises the issue of the relative efficiency of the two approaches. There are a variety of incentives that firms have to adopt corporate governance practices voluntarily.

There are two families of regulations and products: those relating to the character of products (be they raw materials, intermediates, final goods, or services), and those relating to the character of the processes involved in the production of these products. There are important differences in the motivations of public and private stakeholders in imposing regulations and standards in businesses.

Standards in the supply chain can be multifaceted and complex and therefore, corporates are adopting the Triple Bottom Line Approach for resolving the issue of quality and standards. Standards targeting the economic bottom line are used to drive continuous improvement through the chain by demanding higher standards and certifications from its suppliers. The firms also need to meet their Social Bottom Line (e.g., labour standards, ethical trade) and Environmental Bottom Line (e.g., forestry sustainability, organic standards) to determine their economic performance and social license to operate in final markets. The regulations and standards which determine market entry in high income markets have a demonstrable and often positive impact in achieving the Sustainable Development Goals (SDGs). Regulations and standards can be an absolute barrier to entry in Global Value Chains (GVCs) - because products do not meet regulatory requirements and cannot be internationally traded. Therefore, it is imperative to set economic, social, and environmental standards that suppliers are unable to meet, hence excluding sub-standard suppliers from global markets or particular market niches.

First of all, it is important to know the difference between Codes of Conduct and Voluntary Sustainable Standards (VSS). Codes of Conduct can be developed internally or externally. They are a set of practice guidelines characterized by flexible implementation rules that tend to lack enforcement

Alternative Trajectories in CSR mechanisms and may not have audit or reporting criteria. VSS are here defined as the independent and publicly determined standards that have, as primary criteria of compliance, multiple aspects of sustainability defined as specific social, environmental and economic guidelines that feature transparent auditing and more credible (typically external) third party enforcement mechanisms (Geovannucci et al., 2014). More and more firms are now employing VSS so as to capture the benefit of market positioning which appeals to consumer sentiments and can contribute to brand loyalty.

2.3.1 Reasons for increasing adoption of VSS by firms:

1. Conscious consumers having strong interest in personal health as well as awareness about social and environmental concerns in the place of origin
2. Changing business environment with increased dependence of corporate reputation on subsidiaries' operations and also on those of each company in its global supply chain.
3. An emerging regulatory environment with strong rules and regulations and greater food safety requirements such as traceability in food supply chains and more stringent sanitary and phytosanitary restrictions.
4. Increased realization of the strategic importance of sustainability reporting and communications which exposes the corporations to greater level of public scrutiny and can build or tarnish reputations.

2.3.2 Relationship Between Firms and Standards

Some of the important sustainability standards that prevail internationally include Fairtrade International and FairTrade USA, Forest Stewardship Council, Rainforest Alliance and UTZ Certified. Among the various sustainability criteria covered by these standards, the most covered are environmental and social criteria. There is often a dynamic tension between firms and the voluntary sustainability standards. Some of the standards require the firms to change their practices which may change their cost structures. Sometimes the VSS may not be able to meet the firm's needs. Some of the big firms end up creating their own standards. For example, in early 2000s, Starbucks had declared that they are leading buyers of Fairtrade coffee and this claim brought them under the attack of consumers and student's activists who asserted that only a very small percentage of their coffee purchases were Fairtrade certified. Subsequently the firm came up with its own private standard called Coffee and Farmer Equity (CAFÉ) practices.

2.3.3 Difference between Public and Corporate Standards

As discussed earlier, some corporations choose to create their own standards either independently or as a part of some association. There are supermarkets that create their own labels. Most of such standards are business to business (B2B) standards like the Ethical Tea Partnership (ETP), The Round Table Sustainable Palm Oil (RSPO) and Global GAP and they establish minimum guidelines that need to be followed.

There are distinctions between consumer facing VSS and B2B standards or codes of conduct. The latter are typically more concerned with quality, food safety, and traceability than with more comprehensive aspects of sustainability and they have not needed to prioritize transparency and independent audits. While they provide a useful base, most of the B2B standards are modest on social and environmental requirements when compared to the consumer-oriented standards and set the bar for compliance at a fairly low level (Giovannucci et al., 2014)

Most of these B2B standards differ from the VSS values in several ways:

1. These standards are developed and imposed on the producers and supply chains without taking much input from the producers in their design.
2. As there is no third party certification, there is every possibility that the private firm could dilute, alter or not fully apply the standards
3. Cases where sustainable production practices lack adequate remuneration, these standards could act as barriers to entry for producers
4. They generally are not transparent and lack accountability thus reducing them as mere market mechanism that drives sustainability.

2.3.4 Some Important International Standards

These are some of the important international standards:

- OECD Guidelines for Multinational enterprises
- UN Guiding Principles
- Global Reporting Initiative
- ISO 26000 – Social Responsibility
- Voluntary Principles
- United Nations Global Compact
- Equator Principles
- IFC Performance Standards
- Extractive Industries Transparency Initiative
- UN Principle for Responsible Investment

2.4 MARKET MECHANISM AND CSR

To help countries meet their targets for reducing greenhouse gas emissions, and to encourage the private sector and developing countries to contribute to emission reduction efforts, negotiators of the 1997 Kyoto Protocol included three market based mechanisms: Emissions Trading, Joint Implementation and the Clean Development Mechanism (CDM) (Kinkead, 2012).

2.4.1 Emissions Trading

The signatories of the Kyoto Protocol have accepted targets for either limiting or reducing their emissions. These targets are expressed as levels of allowed emissions, or assigned amounts, at over the 2008-2012 commitment period. These allowed emissions are divided into assigned

amount units. Article 17 of the Kyoto Protocol allows emissions trading in which, countries that have not used the emissions permitted to them are allowed to sell their excess capacities to the countries that are over their targets. Thus a new commodity was created for trading in the form of emission reductions. Since the principal greenhouse gas is carbon dioxide, this trading is generally referred to as carbon trading. This market in which carbon is traded is known as the carbon market.

There are also other units which may be transferred under the scheme. Each of these units is equal to one tonne of CO2. These units are (UNFCCC, 2020):

- “A removal unit (**RMU**) which is based on the land use, land use change and forestry (LULUCF) **activities such as reforestation**
- **An emission reduction unit (ERU)** which is generated by a joint implementation project
- A certified emission reduction (**CER**) which is generated from a clean development mechanism project activity”

2.4.2 Joint Implementation

‘Joint implementation’ is a mechanism defined in Article 6 of the Kyoto Protocol, which allows a country with an emission reduction or limitation commitment under the Kyoto Protocol to earn emission reduction units (ERUs), each equivalent to one ton of CO2, from an emission reduction or emission removal project in another signatory country which it can count towards meeting its committed target. Joint implementation offers the signatory countries a flexible and cost efficient means of fulfilling a part of their Kyoto commitments, while the host country benefits from foreign investment and technology transfer (UNFCCC).

2.4.3 Clean Development Mechanism

Article 12 of the Kyoto Protocol is about The Clean Development Mechanism (CDM). It allows a country with an emission reduction or emission limitation commitment under the Kyoto Protocol to implement an emission reduction project in developing countries. Such projects can earn saleable certified emission reduction (CER).

Clean Development Mechanism (CDM) has incorporated sustainable development as one of their objectives. This objective gives companies an increasing motivation to contribute to sustainable development through their corporate social responsibility (CSR) (Lazaro and They, 2017).

Activity 2

Review some case studies on how different market mechanisms have contributed to sustainable development through CSR. Write any one of them.

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Example

India has a large potential to earn carbon credits. India is currently the fourth largest GHG emitter in the world, although its per capita emissions are less than half of the world’s average. India has generated 1,77,360,206 CER’s through CDM till 2014 and India stands second in the world in terms of CDM projects registered and issuance of CER’s next to China. Delhi Metro Rail corporation has become first ever railway project in the world to claim carbon credits because of using regenerative braking in its rolling stock. DMRC reduces 30% electricity consumption with regenerative braking system in its trains. DMRC claimed 4,00,000 CERs for a 10 year crediting period starting December, 2007 when the project was registered by the UNFCCC. This converts to 1.2 crore per year for 10 years. DMRC has also been certified in June, 2011 by the United Nations body as the first Metro Rail and Rail based system in the world to get carbon credits for reducing GHG emissions as it has helped to reduce pollution levels in the city by 4.5 lakh tons every year, thus helping in reducing global warming. DMRC so far has helped in removing more than 91 thousand vehicles from the roads of Delhi on daily basis. Accordingly, DMRC’s second CDM project has been developed, based on the shift of public travels in cars / buses and other means of road transport to the metro trains.

Source: (Maheshwari and Goyal, 2015)

Check Your Progress - 2

- Notes:** a) Write your answers in about 50 words.
 b) Check your answer with possible answers given at the end of the unit.

1. What is the carbon market?

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2. What is a Clean Development Mechanism?

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2.5 LET US SUM UP

For raw material supply chains to be more sustainable, it is important to ensure equitable and ethical supply terms for the producers of these raw materials. In this unit you have read about issues and challenges as well

Alternative Trajectories in CSR as the conditionalities in the raw material production of tea, coffee, cotton and palm. The corporate sector across the globe faces varied public driven regulations of doing business, which has been reduced over the times to facilitate business organizations. In this unit you have also read about the voluntary sustainable standards and their roles. Finally you have read about the three market mechanisms included in the Koyoto Protocol.

2.6 KEYWORDS

Ethical Value Chain - The elements of ethical supply chains include: labour wages and discrimination, human trafficking, green certification, and sustainability.

Triple Bottom Line Approach - The triple bottom line (TBL) is a framework or theory that recommends that companies commit to focusing on social and environmental concerns just as they do on profits.

Sustainable Development Goals - The Sustainable Development Goals (SDGs), also known as the Global Goals, were adopted by all United Nations Member States in 2015 as a universal call to action to end poverty, protect the planet and ensure that all people enjoy peace and prosperity by 2030.

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Common Code for the Coffee Community, The 4C Association, <http://www.sustainable-coffee.net/>

<https://unfccc.int/process/the-kyoto-protocol/mechanisms>

2.8 CHECK YOUR PROGRESS – POSSIBLE ANSWERS

Check Your Progress - 1

Answer 1: Two issues related to sustainable cotton production include:

- i) Use of child labour and other issues related to workers rights. Also, cotton is one of the goods most commonly produced using forced labour. Forced labour exists in nine countries producing 65% of world's cotton.
- ii) Use of genetically modified cotton. In 2016, 64% of the cotton grown was genetically modified. Farmers are unable to use the seeds of GM crops for the next season and become perennially dependent on the MNCs for seeds. Besides, the GM crops are more input intensive.

Answer 2: Some of the sustainability concerns in the seafood markets include:

- 1) Environment: Issues related to greenhouse gas emission, energy use, waste, pollution and water use in fishing and processing activities.
- 2) Human Rights and Labour Practices: Working agreements, working conditions, health and safety, fair wages, human rights.

Check Your Progress - 2

Answer 1: Article 17 of the Kyoto Protocol allows emissions trading in which countries that have not used the emissions permitted to them are allowed to sell their excess capacities to the countries that are over their targets. Thus a new commodity was created for trading in the form of emission reductions. Since principle greenhouse gas is carbon dioxide, this trading is generally referred to as carbon trading. This market in which carbon is traded is known as “carbon market”.

Answer 2: Article 12 of the Kyoto Protocol is about The Clean Development Mechanism (CDM). It allows a country with an emission reduction or emission limitation commitment under the Kyoto Protocol to implement an emission-reduction project in developing countries.