

# The Accountability Framework

## Operational Guidance on Smallholder Inclusion in Ethical Supply Chains

**DRAFT FOR WORKSHOPPING**  
December 2018

### **DECEMBER 2018 DRAFT FOR 'WORKSHOPPING' WITH STAKEHOLDERS**

The Accountability Framework initiative (AFi) is developing a common framework to guide the setting, implementation, and monitoring of supply chain commitments. As part of the Accountability Framework, this draft document represents a working consensus of the AFi partners as well as input from prior consultations involving stakeholders from the private sector, civil society, and government. The partners are sharing this draft publicly and inviting feedback from all interested parties to further build and refine the Framework in a way that reflects the needs and perspectives of those working to bring about responsible supply chains and positive outcomes for people and nature. Based on this consultative process, version 1.0 of the Accountability Framework will be published in early 2019.

For more information, or to provide input during the present workshopping process, please visit <https://accountability-framework.org> or send an email to [contact@accountability-framework.org](mailto:contact@accountability-framework.org)

**DISCLAIMER:** This work product is intended to be advisory only and is not intended to serve as a legal opinion or legal advice on the matters treated. The reader is encouraged to engage counsel to the extent required.

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## PURPOSE & SUMMARY

This Operational Guidance elaborates several of the Accountability Framework Core Principles to specify how companies can effectively engage smallholders in ethical supply chains in a manner that is likely to be mutually beneficial – that is, providing benefits and positive incentives to smallholders while enabling companies to fulfill their supply chain commitments and secure adequate volumes of responsibly produced commodities.

Smallholders produce a high percentage of numerous major commodities, such as cocoa, coffee, palm oil, rubber, and forest products. As such, they form an integral part of the supply chains for many companies dealing in these commodities. For smallholders, participation in supply chains governed by ethical supply chain commitments can provide an opportunity to increase the stability and sustainability of livelihoods while avoiding further deforestation and improving labor practices.

The Accountability Framework does not provide a recommendation regarding the scope or content of company commitments related to smallholder inclusion, as the appropriate approach is highly context specific. Rather, the Framework aims to facilitate smallholder inclusion in responsible supply chains by clarifying how the implementation of company supply chain commitments can be adapted or nuanced to smallholder contexts. This guidance provides elaboration of several aspects of company commitments that may require further consideration when applied to smallholders.

This guidance addresses:

- Definition and characteristics of smallholder producers
- Risk assessment and traceability in supply chains that include smallholders
- The role of smallholder groups in responsible supply chains
- Expectations for company engagement and support of smallholders
- Considerations for addressing non-compliance and retention of smallholder producers

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### 1. The smallholder context

Smallholders play a critical role in the production of many agricultural and forestry commodities. Inclusion of these producers in responsible supply chains is essential to help support livelihoods of rural communities, increase agricultural productivity, avoid displacement of social and environmental impacts, and secure stable commodity supplies. However, there are challenges to ensuring that smallholders adhere to company commitments related to the protection of natural ecosystems and respect for human rights. These include insecure land tenure, insufficient access to inputs or finance, political disenfranchisement, poor access to markets and information, lack of training and support, and lack of economies of scale.

As a result, companies sometimes exclude smallholders from their supply chains due to higher costs of ensuring compliance as well as higher transaction costs and overall levels of risk. However, this exclusion may limit the effectiveness of supply chain commitments, increase the risk of displacing negative impacts to areas outside company control, and carry additional reputational or legal risks. The AFi therefore aims to facilitate smallholder inclusion in responsible supply chains by clarifying how supply chain commitments can be effectively implemented and monitored in smallholder contexts in a manner that is beneficial to smallholders themselves.

To facilitate smallholder inclusion, companies may provide special consideration to smallholders when implementing commitments addressing deforestation, land conversion, and human rights. These considerations include:

- Contextualized implementation of environmental and human rights related commitments for smallholders, which may include smallholder-appropriate guidelines for the level of traceability required, engagement and retention of non-compliant suppliers, and degree of involvement in remedy of past environmental harms.
- Support for smallholder producers, including enabling access to financial services, agricultural inputs, training and technical assistance, support for land titling, and other support programs.

## 1.1 Defining smallholders

The term “smallholder” is defined in different ways in different contexts and by different people and organizations. The Accountability Framework defines this term for the specific purpose of determining when companies may need to develop smallholder-specific policies, practices, or support related to their supply chain commitments.

Smallholders are small-scale agricultural or forest products producers that are distinct from larger-scale producers found in similar contexts by virtue of many or all of the following characteristics:

- high degree of dependence on family labor
- profits accrue primarily to the farm’s or forest’s owner and his or her family
- the farm or forest provides a primary source of income for the smallholder
- production units have a relatively small land footprint (relative to the range of production unit sizes for the given commodity and region)
- household resources allocated to both food crops and cash crops
- relatively low use of agricultural inputs, and generally low productivity and yields
- significant economic constraints, such as lack of capital assets and low access to finance
- significant information constraints, including lack of technical knowledge and low access to market information

Producers with these characteristics are likely to be in a position both to warrant and to benefit from company support or contextualized implementation of company commitments.

Consistent with the criteria and parameters outlined in the above definition, numerous governments, international agencies, policies, and sector initiatives provide more specific and quantitative definitions of smallholders, which may differ depending on location, land use type, and commodity. Globally, smallholders are often defined as cultivating less than two hectares (ha) of land, although some definitions set thresholds of 5 or 10 ha, and in certain production systems (e.g., livestock raising) significantly larger production units may be considered as smallholdings. Many initiatives, including certification programs, provide specific definitions or eligibility criteria to identify smallholder producers, while others have generic definitions subject to national interpretation. For instance, the Roundtable on Sustainable Palm Oil (RSPO) standards provide that smallholder farms may be defined as up to 50 ha subject to national interpretation; the Indonesian interpretation has set this threshold size at 25 ha while interpretations for Ghana and Malaysia specify 40 ha.

Where companies participate in certification programs, sector programs, or jurisdictional initiatives that define smallholder production, they may adopt those definitions when they appropriately reflect the above characteristics as relevant in the given context. Where such contextualized definitions are not available, national definitions may likewise be used when congruent with the above criteria in the given context. Where none of

these exist, the above generic characteristics may be interpreted for each context according to these same considerations.

As a final note, there is wide variation in the extent to which smallholders are integrated into commodity markets. Some smallholders produce only for subsistence consumption or informal trade; others sell a portion of their production into more formal local or regional markets; and others are fully integrated into regional or global commodity supply chains. Company supply chain commitments – and therefore the scope of the AFI – generally address only smallholders engaged in the production of commodities that are traded regionally or globally who are, or could potentially become, suppliers to company supply chains. In practice, however, companies will likely need to engage with smallholders who carry out multiple types of production. This includes commodity-supplying smallholders who also produce subsistence crops, as well as smallholders in the surrounding area whose production may be directly or indirectly affected by company operations or sourcing activities.

## 1.2 Independent versus company-affiliated smallholders

This Operational Guidance applies most directly to smallholders that are fully or largely independent of the buyers and aggregators to whom they sell. While independent smallholders can have long-term purchase arrangements with their buyers, generally buyers do not provide these smallholders with regular and long-term support (e.g., farm inputs or technical assistance), nor do they prescribe specific types of agronomic or land management practices that the smallholders must follow. For these reasons, independent smallholders are largely autonomous in their decision-making, but may lack the resources and knowledge to identify or implement responsible practices included in company supply chain commitments.

In contrast to independent smallholders, company-affiliated smallholders (variously called “scheme smallholders,” “plasma smallholders,” “outgrowers,” or by other terms) typically have a long-term or permanent selling relationship with a given buyer and receive significant levels of inputs, support, and/or requirements or mandates from that buyer. In some cases, smallholders are absentee landowners whose land is managed entirely by plantation companies. In these scenarios, the company with whom the smallholder is affiliated has a significant level of influence over how the smallholder’s land is managed.

Because of the company’s higher degree of influence and/or support in “affiliated” scenarios, affiliated smallholders are generally expected to comply with the same standards as the larger-scale operations of that company. By contrast, independent smallholders are more likely to experience constraints in knowledge, inputs, capital, or economic position that hinder their ability to understand and fulfill all elements of company supply chain commitments. This Operational Guidance therefore applies primarily to independent smallholders, and is intended to clarify appropriate pathways for fulfilling or progressing toward commitments in view of the constraints that these smallholders may face.

## 2. Traceability and risk assessment in a smallholder context

Core Principle 2 specifies that companies sourcing raw materials or derived products should have sufficient supply chain visibility or control to assess compliance with commitments. Where risk levels are moderate, high, or unknown, the following applies:

Core Principle 2.2: Primary processors and traders know the origin of raw materials to the level of the farm, estate, plantation, ranch, or forest management unit. **For smallholders, origin is known at least to the level of the farmer group or the smallest legal jurisdiction, with more detailed mapping conducted where necessary to assess fulfillment of commitments.** If traceability to these levels is not initially available, then it is progressively improved to these levels over a pre-defined timeline, prioritizing the riskiest settings.

In smallholder contexts, the appropriate level of traceability and control to fulfill this Core Principle depends on whether smallholder groups and/or upstream actors such as primary processors or traders are effectively ensuring compliance of the smallholders within these groups or supply chains. This may be done through monitoring and control systems, including certification. Downstream companies, in turn, will often need to depend on certification programs or upstream companies and their control systems to assess, manage, and communicate risk effectively. In these cases, downstream companies' obligation is to ensure that the proper supplier requirements, support, and oversight are in place (see *Operational Guidance on Supply Chain Management*).

## 2.1 The role of smallholder groups

There are often technical challenges and significant costs associated with tracing products to the level of individual smallholders. Smallholder group structures can be an effective way to help address traceability needs while managing risk of non-compliance by smallholder producers. Effective group structures can also help support smallholder wellbeing and farm productivity by providing members with training knowledge, inputs, resources, and access to markets. For these reasons, a primary objective of smallholder engagement should be to facilitate the entry of smallholders into groups that are effective in helping smallholders to adopt best practices, continuously improve outcomes, and fulfill supply chain commitments of commodity buyers.

Smallholder groups include cooperatives, farmer associations, and groups managed by traders, processors, or government initiatives. These groups may serve different purposes, such as collective processing and marketing of their members' products; provision of inputs and training to group members; political alignment and advocacy to advance the members' interests; or compliance with external standards or market demands (e.g., certification programs).

In the context of responsible supply chains, one important function of smallholder groups is to operate control systems that serve to assess compliance, manage risk, and document performance of their members relative to external standards or other company commitments. Requirements for such control systems are usually codified in some detail as part of certification programs that include a group certification model. However, effective control systems can also be developed outside of certification programs to facilitate the participation of non-certified smallholders in responsible supply chains. Whether used in the context of certification or otherwise, key elements of effective smallholder group control systems include:

1. Minimum requirements for group membership, which may include compliance or time-bound plans for progressing toward compliance with external standards or company commitments
2. Maintenance of a current inventory of group members and their location (at least point coordinates, if not production unit boundaries) and other basic characteristics (e.g., production unit size, production volume, and owner data)
3. Procedures for internal monitoring or auditing to assess members' compliance
4. Policies, procedures, and support mechanisms to foster time-bound corrective actions for members that are found to be non-compliant, which may also include actions taken by the group manager to address collective challenges of the members
5. Policies and procedures to exclude group members that incur serious non-compliances or fail to achieve time-bound progress to address other non-compliances
6. Internal controls on traceability, product mixing, and volume reconciliation to ensure that all product sold by the group or its members actually originated on members' production units that are subject to the group control system

7. Electronic record-keeping to facilitate risk management and improvement processes and to make data readily available to second parties (e.g., buyers) or third parties (e.g., external auditors) to assess and validate levels of compliance or progress as well as the effectiveness of the control system itself

Where smallholder groups operate effective control systems, the risk of severely non-compliant smallholders entering the supply chain is generally managed and contained at the group level, and traceability beyond the level of the group may be unnecessary. However, group-managed control systems can vary considerably in the level of rigor and precision with which they assess and control the compliance of their members with regard to key environmental and social requirements. It is ultimately the responsibility of intermediate and downstream buyers to understand the capabilities and limitations of smallholder group control systems, and to provide for supplemental risk assessment, monitoring, verification, and support functions where these control systems do not provide full assurance of internal traceability, compliance monitoring, and appropriate corrective action relative to company commitments.

Where groups do not operate control systems – or where their control systems do not effectively provide for the functions listed above – they may nevertheless have knowledge about and relationships with their members that may be used to help assess and manage compliance or risk across the group. For instance, upstream companies may work with group managers as a first point of engagement to conduct risk assessments and gap assessments. The results of these assessments can then inform targeting of further efforts to address any identified risks or non-compliances related to company commitments, as well as challenges related to smallholder productivity and wellbeing. Several frameworks and tools are available or in development that provide guidance on assessment and risk management in a smallholder context (see Box 1).

## 2.2 Supplemental action for smallholder traceability and control systems

Commodity-buying companies are ultimately responsible for achieving and demonstrating fulfillment of their commitments. Therefore, when smallholder group structures are not adequately providing this function, buyers may need to take supplemental action to fulfill their commitments. Such action is typically required when the smallholder group is not located in a low-risk area, is not certified, and does not operate a control system that effectively fulfills at least the above-stated seven functions. For instance, if the group cannot provide accurate or consistent information about group membership and members' locations, does not have clear policies for membership and member exclusion in the case of non-compliance, or does not operate effective controls for preventing double-selling or product laundering, then supplemental action by buyers is typically warranted. Such action may include steps to either support the capacity of the group to improve their control mechanisms, or else intervene directly to carry out risk assessment and gap assessment, conduct traceability to the production unit, and help develop engagement plans to address non-compliance where required. Support and capacity building may include, for example:

- Training of the group manager on effective control system functions
- Support for smallholder farm mapping and assessment to document the sources and attributes of the production units of origin
- Additional external (second- or third-party) auditing of the group's control system
- Support to improve internal traceability and minimize volume fraud and product laundering

When companies source from individual smallholders who do not belong to groups, and are not subject to effective control systems by direct buyers (e.g., a mill or local trader), downstream buyers typically must provide traceability to the production unit level to assess compliance of these individual smallholders. This includes the farm location documented as point coordinates or farm boundaries. In the absence of either sufficient controls or full traceability, companies should engage with their suppliers to institute the necessary improvements to traceability and control systems, as elaborated in the *Operational Guidance on Supply Chain Management*. If

these efforts do not result in timely improvements, then such smallholders may need to be excluded from responsible supply chains.

### **Box 1: Risk assessment and mitigation through smallholder initiatives**

Several certification standards, sectoral initiatives, and other programs have developed or are developing procedures for guiding smallholder engagement in responsible supply chains. The initiatives featured in this box, and other similar initiatives, may be used to help fulfill company commitments in accordance with the Accountability Framework by helping to assess and manage risk of non-compliance and support improvement processes.

- The SHARP Responsible Sourcing from Smallholders (RSS) framework<sup>1</sup> provides guidance to companies to aid in the prioritization and implementation of risk mitigation measures and activities to address smallholders' needs for support. It also includes field guides on implementation, documentation, monitoring, and review of such action plans. This type of stepwise approach to assessment, implementation, and review provides a basis for companies to document improvement in smallholder practices and progress toward compliance with commitments.
- Several forest certification programs offer group certification approaches that allow hundreds or thousands of small forests managers to become certified under one certificate. This approach increases accessibility and reduces cost of certification to small-scale operators, while helping to support information dissemination, cooperation in forest management, and increased capacity for remediation or preventative actions.
- The draft Roundtable on Sustainable Palm Oil (RSPO) smallholder standard, currently in development, proposes a simplified process for achieving RSPO certification for groups of independent smallholders. This draft standard provides a modified set of principles, criteria, and options for verification tailored to the smallholder context. The standard allows for a phased approach to compliance, with generation of credits for partial compliance to provide early incentives for smallholders to work toward full compliance.
- The High Conservation Value (HCV) Resource Network has developed procedures to help RSPO and Better Cotton Initiative smallholders apply the HCV approach based on use of a simple risk-assessment questionnaire and adoption of precautionary management practices. Similar work is in process to support smallholders' application of the HCV approach in the context of the Bonsucro and Aquaculture Stewardship Council certification programs.
- The draft High Carbon Stock Approach (HCSA) for smallholders and Serikat Petani Kelapa Sawit's HCV-HCS guide for smallholders, which build on RSPO's simplified HCV approach, provide a streamlined process to assess HCVs and HCS forests in smallholder contexts and to manage risk through precautionary practices where the probability of HCVs and HCS forest presence is not high. This smallholder-oriented approach is intended to satisfy market-driven requirements to protect HCVs and HCS forests.

## **3. Smallholder engagement, support, and communication**

Core Principle 3.2 specifies that companies with long-term or recurring buying relationships with suppliers should support them in fulfilling company commitments, with priority given to smallholders (and others who may require more assistance) to avoid their exclusion from supply chains. Engagement with smallholder producers has the potential to greatly increase a company's positive environmental and social impact, and in many contexts is essential to halting deforestation and conversion of natural ecosystems, respecting human rights, and improving the wellbeing of rural communities. To enable smallholders to participate in ethical supply chains and achieve compliance with company commitments, companies may need to provide various

<sup>1</sup> <https://www.sharp-partnership.org/RSS>

kinds of support to improve economic outcomes and reduce financial risk for resource-poor and risk-averse smallholders and to help decrease transaction costs of smallholders participation. The absence of such support or engagement may negatively affect smallholder livelihoods (e.g., if smallholders are excluded from certain markets) or exacerbate environmental or social harms (e.g., if smallholders sell into alternative supply chains that are not subject to responsible sourcing commitments).

Companies should, in all cases, operate with the understanding that smallholders retain the right to make their own decisions regarding the use of their land, their participation in commodity supply chains, and their interests in balancing livelihood and conservation considerations (*See Operational Guidance on Long Term Protection*).

Smallholder engagement may be carried out in collaboration with other buyers sourcing from the same smallholders, as well as with other private-sector initiatives, government programs, certification programs, or the efforts of NGOs and local civil society organizations (CSOs). For instance:

- NGOs and CSOs can operate as intermediaries between companies and smallholders, with the company supporting these organizations to provide smallholders with training, organization, sensitization, communications, and promote positive interaction with government and other actors.
- Downstream companies, which may have more difficulty directly supporting smallholders across their whole supply base, can collaborate with governments to develop policies that support the entry of low-capacity smallholders into supply chains and ensure that communities benefit more broadly from entry into commodity supply chains.

### 3.1 Support for smallholders

Smallholders face a range of limitations and challenges in achieving and sustaining environmentally and socially responsible production, and in demonstrating sufficient evidence of such performance. The most appropriate forms of company support to overcome these barriers will depend on the context of the smallholder producers (e.g., commodity, location, access to markets, and specific production constraints that the smallholders face) as well as the company’s position in the supply chain. Table 1 provides examples the types of support that companies should consider offering to facilitate smallholder inclusion in responsible supply chains.

<b><i>Companies may provide support to enable smallholders to:</i></b>	<b><i>Types of support that may be appropriate:</i></b>
Enter into or remain part of responsible supply chains	<ul style="list-style-type: none"> <li>• Enter into long-term purchase contracts that assure future revenue, thus facilitating smallholders’ investment in improved practices</li> <li>• Provide or facilitate access to financial services and credit</li> <li>• Support for land titling and other legal needs</li> </ul>
Derive greater benefits from sustainable management practices and participation in responsible supply chains	<ul style="list-style-type: none"> <li>• Provide price premiums for compliant commodity production</li> <li>• Facilitate participation in carbon markets or other payment for ecosystem services (PES) programs</li> </ul>
Enter into group arrangements to facilitate production, marketing, certification, and risk management	<ul style="list-style-type: none"> <li>• Provide information and technical support to smallholders to facilitate their participation in group structures</li> <li>• Provide organizational support and capacity building to group managers to develop, monitor, and enforce policies and requirements for group membership</li> </ul>



	<ul style="list-style-type: none"> <li>• Provide technical support to groups to improve control mechanisms, including mapping, risk assessment, and data management regarding group members and their compliance levels</li> <li>• Facilitate access to financial services and credit for groups to improve management, infrastructure (e.g., for product storage and transportation), and monitoring capabilities</li> </ul>
Improve yields and production practices to increase stability and profitability of commodity production	<ul style="list-style-type: none"> <li>• Provide, pre-finance, or facilitate access to agricultural inputs (e.g., fertilizers and high-quality planting stock)</li> <li>• Provide or facilitate technical support and training</li> </ul>
Achieve compliance with or progress toward company commitments	<ul style="list-style-type: none"> <li>• Provide information to raise awareness of buyer expectations regarding production practices and social and environmental performance</li> <li>• Contribute financial resources or technical support for risk assessment, monitoring, verification, and reporting</li> <li>• Contribute financial resources or technical support for restoration, remediation, or conservation activities</li> <li>• Provide capacity-building and support for identifying violations of workers' rights and improving labor practices</li> </ul>

In most cases, downstream companies will not be in a position to provide direct support to all smallholder producers in their supply chain. In these cases, support may be channeled through upstream actors such as mills and traders, or by working in collaboration with certification programs and sector-based or jurisdictional initiatives that support smallholders, or by participating in government or NGO programs to provide technical or material support to smallholders working to enter or remain in responsible supply chains. Upstream companies are more commonly in a position to directly assess the needs of producers and target support appropriately.

### 3.2 Communication

A key limitation to smallholder participation in responsible supply chains is the lack of access to clear information about the nature, applicability, and timeframe of company supply chain commitments. Without appropriate and timely information about company commitments and other requirements, smallholders may be unable to meet these requirements or may incur non-compliances (such as deforestation) that could make them ineligible for future participation. Companies therefore should work to provide information to smallholders in a timely manner and appropriate formats to allow them to make informed decisions and to anticipate and achieve compliance with company commitments.

Communication through smallholder group management structures can be an effective means of outreach to group members. Downstream companies may identify upstream supply chain actors such as mills or traders as potential pathways for communicating company commitments to both smallholder groups and independent smallholders. Downstream companies can also collaborate with NGOs or certification programs to support or implement specific communication pathways such as the use of SMS or other messaging services, training of lead farmers who can aid in information dissemination, or other proven approaches to information and technology transfer.

Smallholders also face barriers in communicating their needs to commodity buyers and potential supporters or partners. Company engagement strategies should therefore also consider developing or improving mechanisms for smallholder groups to provide feedback on company policies and programs and to incorporate

information from smallholders into decision-making. For example, interviews or focus groups with smallholders or group managers can enable companies to better understand smallholders' needs and constraints. Upstream companies who interact with farmers may provide fora for communication and feedback, while downstream companies can survey representative samples of their smallholder suppliers to assess needs and target resources and support accordingly.

## 4. Addressing non-compliance of smallholder suppliers

As indicated in [Core Principle 3](#), companies are expected to manage non-compliance in their supply base by engaging, suspending, or excluding non-compliant suppliers, as appropriate to the nature of the non-compliance(s) and other circumstances. The *Operational Guidance on Supply Chain Management* elaborates the factors that buyers should consider when determining the appropriate course of action. These factors include the severity, extent, and persistence of the non-compliance(s) as well as the degree of culpability and the past and current practices of the supplier. The following guidance provides further specificity about how those criteria may be understood and assessed when sourcing from suppliers who are smallholder producers. This information can guide companies when making decisions regarding:

- when to retain existing non-compliant smallholder suppliers, what kinds of continuous improvement should be expected from retained suppliers, and what kinds of support should be provided to facilitate such improvement;
- when to suspend or exclude existing non-compliant smallholder suppliers;
- when to initiate new sourcing relationships with smallholder suppliers that may have a certain degree of non-compliance; and
- how to report progress toward or compliance with company commitments under the different scenarios discussed here.

### 4.1 Assessing non-compliance in a smallholder context

In the case of non-compliant smallholders or smallholder groups, in addition to the general guidance provided in the *Operational Guidance on Supply Chain Management*, companies should consider the following **three sets of factors** to help determine the appropriate course of action:

1. Are smallholder groups managing their members effectively to prevent future non-compliance? Conditions indicating that this is the case include:
  - a. The group effectively maintains minimum requirements for group membership (e.g., specified group regulations and procedures) that align with commitments of their buyers.
  - b. Neither the group nor its members receive support, assistance, financial inducement, or encouragement from a direct or indirect buyer, financier, or other party to expand or modify production practices in a way that would increase non-compliance, such as expanding production into existing forests or other natural ecosystems.
  - c. The group effectively communicates to its current and prospective members about requirements to comply with company commitments.
  - d. The group provides support and incentives for producers to achieve compliance with these commitments.
  - e. The group monitors, documents, and reports on progress of members toward compliance including, when appropriate, exclusion of noncompliant members.
2. Are the smallholders fully or largely in compliance with company commitments? Conditions indicating that this is the case include:

- a. All or nearly all of the given set of smallholders comply or mainly comply with the company's commitments.<sup>2</sup>
  - b. To the extent there is non-compliance, the group and its members demonstrate substantive progress toward compliance over time.
  - c. To the extent that non-compliance with deforestation-free or conversion-free commitments is due to past land use change that has not been properly remedied, these past actions were carried out in the absence of information that they were contrary to company commitments and without support or encouragement from buyers.
3. Where appropriate and feasible, are the subject smallholders or the groups of which they are members carrying out restoration or remediation of past harms? Conditions indicating that this is the case include:
    - a. Where smallholders converted natural ecosystems contrary to company commitments, context-appropriate restoration or compensation is conducted. This may include protection of remaining natural ecosystems under threat of conversion; restoration of natural ecosystems where feasible (e.g., riparian zones and areas of marginal productivity); and/or changes in land management and production regimes that help protect ecosystems and improve conservation value while also supporting commodity production (e.g., introduction of native shade trees, agroforestry systems, buffer strips, etc.).
    - b. Where smallholders caused or contributed to human rights violations, appropriate remedy is pursued according to the *Operational Guidance on Remediation and Access to Remedy*.
    - c. When the restoration or remediation activities that would otherwise be required to address past harms (per the *Operational Guidance on Remediation and Access to Remedy*) are beyond the capacity of smallholders and/or groups, they seek support from their buyers and/or government entities to facilitate such actions. (Direct buyers of smallholder-sourced products should be responsive to these requests and provide such support, as elaborated in section 3. Indirect buyers should assess the extent to which their suppliers have programs or systems in place to provide (or require their suppliers to provide) support to smallholders to carry out appropriate restoration or remediation activities (see *Operational Guidance on Supply Chain Management*.)

## 4.2 Taking actions to engage, retain, suspend, or exclude non-compliant smallholder suppliers

All of the above factors should be considered together and interpreted based on the given context when making decisions about the management of smallholder suppliers. These multiple factors may also be weighed differently when determining how to manage existing non-compliant smallholder suppliers versus when deciding whether to initiate new buying relationships.

Where commodity-buying companies already source from smallholders, they are generally encouraged to retain such suppliers even when they are not entirely compliant with company commitments, provided that:

- a) the severity, extent, and persistence of non-compliances are not great enough to clearly warrant suspension or exclusion (based on the parameters outlined in Section 4 of the *Operational Guidance on Supply Chain Management*); and

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<sup>2</sup> There is no single generic, quantitative threshold for this level of compliance. However, as an indicative example, it would typically be reasonable for companies to retain a smallholder group in which 10% of members had engaged in post-cutoff date conversion, provided that other factors (and particularly factor 1c) were fulfilled. Similarly, companies would typically be encouraged to maintain purchasing relationships with smallholders that utilize a limited amount of child labor based on customary practices, and in these cases would be expected to work with these smallholders to eliminate and remedy such non-compliance through best practices such as Child Labor Monitoring and Remediation Systems (CLMRS).

- b) smallholder groups have fulfilled factor 1 in Section 4.1 above, or are taking adequate steps to do so within a short period of time; and
- c) smallholders have fulfilled, demonstrated substantive progress toward, and/or have documented and are implementing plans toward fulfilling components of factors 2 and 3, above.

When sourcing from smallholders or smallholder groups that are not fully compliant, buyers should engage these suppliers directly or indirectly (i.e., through intermediaries such as traders that have a more direct relationship with the smallholders) as described in Section 5 of the *Operational Guidance on Supply Chain Management*. Because of the different challenges and constraints that smallholders often face, buyers may need to provide a higher degree of support, technical assistance, or incentives than for larger-scale producers. This could include, for instance, technical assistance to improve group administration, monitoring, and control systems; support to develop action plans to improve compliance and remediate past harms, if necessary; and, in some cases, direct monetary or in-kind assistance to overcome specific barriers to compliance. When engagement pathways include traders or other intermediaries, companies may need to provide support and/or incentives to those entities as well.

Assuming such support is provided, and smallholders are allowed adequate time to implement changes in their practices, non-compliant individual smallholders who are not able to demonstrate compliance or significant progress within a reasonable period of time may face suspension or exclusion from responsible supply chains. Likewise, if smallholder groups do not institute adequate controls to identify non-compliance within their membership, ensure high overall levels of compliance or significant progress toward it (factor 2), and avoid the addition of new members who are substantially non-compliant, then the entire group may face suspension or exclusion from responsible supply chains.

Companies should generally avoid initiating new sourcing relationships with smallholders and smallholder groups that have one or more of the following characteristics:

- do not have effective management systems in place for preventing future non-compliance (addressing all components of factor 1);
- demonstrate severe, extensive, or persistent non-compliance with company commitments (based on the parameters outlined in Section 4 of the *Operational Guidance on Supply Chain Management*), with these characteristics assessed across the full membership in the case the smallholder groups (factor 2); or
- do not, at a minimum, demonstrate willingness to remedy past harms when appropriate and feasible (factor 3).

Companies are encouraged to engage with smallholders and smallholder groups that have these challenges or limitations to address these issues, improve management systems, and resolve non-compliances, with the intention of future inclusion in supply chains. However, companies should not begin purchasing from these producers until all three of these factors have been resolved.

### **4.3 Reporting and claims for commodity volume sourced from smallholders**

Regardless of the decisions that companies take to retain, engage, and/or exclude smallholder suppliers based on their given level of compliance, companies are expected to issue truthful reporting regarding the level of compliance of their smallholder suppliers and any corresponding improvement processes that are being pursued. Such reporting is important not only to track progress and drive accountability relative to company commitments; it also enables companies to communicate to their stakeholders why specific groups of suppliers have been retained or excluded, and how the company is using its influence to help improve compliance and smallholder wellbeing. Such communication can help foster mutual understanding and support more constructive and collaborative approaches to smallholder inclusion.

If segments of the company's smallholder sourcing base have different levels of compliance or progress related to different elements of the company's commitment (e.g., no-deforestation, no-conversion, and respect for human rights), then these distinctions should be differentiated in the reporting. For the purpose of public-facing or business-to-business reporting, companies should generally report on their smallholder sourcing base as follows:

- **Compliant:** product volume sourced from smallholders may be reported as compliant where the subject smallholders fully comply with the company's commitments or where they are members of groups that:
  - i. Meet all the criteria in factor 1, above; and
  - ii. Meet all or most of the criteria in factors two and three, and have shown substantive progress toward meeting any unfulfilled criteria.
- **Progressing:** product volume sourced from smallholders that have a significant degree of non-compliance may be reported as progressing toward compliance where they are members of smallholder groups that meet all the criteria in factor 1, and have documented and are implementing a plan to fulfil other applicable criteria in factors 2 and 3.
- **Not compliant:** product volume sourced from smallholders that have a significant degree of non-compliance and are not members of groups taking the above-mentioned actions must be reported as non-compliant with company commitments. In these cases, the company should explain its reason for retaining these non-compliant suppliers and summarize its time-bound plan for moving these suppliers toward compliance.

In addition to the above, companies are also encouraged to report on the nature and extent of their activities, financial and in-kind support, communication, and engagement with smallholder producers to address non-compliance and support smallholder inclusion and wellbeing. Such reporting should be in quantitative terms, when appropriate, to characterize the scale of support or engagement in relation to the size of the company's smallholder supply base or to the current level of non-compliance.