**Inter-Parliamentary Union**
128th Assembly and related meetings
Quito (Ecuador), 22 – 27 March 2013
www.ipu2013ecuador.ec

Second Standing Committee on
Sustainable Development,
Finance and Trade

C-II/128/R
3 December 2012

# FAIR TRADE AND INNOVATIVE FINANCING MECHANISMS FOR SUSTAINABLE DEVELOPMENT

***Report* submitted by the co-Rapporteurs**
***Mr. F.-X. de Donnea (Belgium) and Mr. R. Chitotela (Zambia)***

## INTRODUCTION

1. Fair trade is about better prices, decent working conditions, local sustainability, and fair terms of trade for farmers and workers in the developing world. By requiring companies to pay above market prices, fair trade addresses the injustices of conventional trade, which traditionally discriminates against the poorest and weakest producers.

2. This means a stable price that covers their production costs, along with a premium that their organization will be able to re-invest either in the business or in social and environmental schemes among the wider community.

3. By helping to increase the returns for producers of goods and reduce the cost of inputs either through a reduction of market power abuse or simply through economies of scale in purchase, fair trade addresses the improvement of the quality of life through the organizations that support small-scale producers.

4. At the International Conference on Financing for Development, held in Monterrey in March 2002, the international community recognized "… the value of exploring innovative sources of finance provided that those sources do not unduly burden developing countries".

5. The Doha Declaration on Financing for Development (December 2008) recognized "the considerable progress made since the Monterrey Conference in voluntary innovative sources of finance and innovative programmes linked to them".

6. The Fourth High level Forum on Aid Effectiveness (Busan, December 2011) pledged to "…further develop innovative financial mechanisms to mobilize private finance for shared development goals".

7. Since 2002, there has been strong and increasing political support at the global level for the concept of innovative financing for development: the "Leading Group on Innovative Financing for Development" (http://www.leadinggroup.org) has done a lot of ground-breaking work on this subject. Today, the Leading Group consists of 63 Member States and a number of international organizations (FAO, IMF, OECD, etc.) and non-governmental organizations. The Leading Group pioneers pilot solutions aimed at responding to the international community's call for progress on the Millennium Development Goals (MDGs).

8. The Final Declaration of the MDG Review Summit, adopted by the United Nations on 22 September 2010, refers explicitly for the first time to the role of innovative financing to achieve the MDGs, as well as to the work of the Leading Group. Subsequently, on 20 December 2010, the UN General Assembly adopted resolution 65/146, on Innovative mechanisms of financing for development, operative paragraph 6 of which "*Highlights* the considerable progress in innovative sources of financing for development achieved to date, and stresses the importance of scaling up present initiatives and developing new mechanisms, as appropriate [;]".

**DEFINING FAIR TRADE**

9. Fair trade is a way of doing business that ultimately aims to keep small farmers and producers as active participants of the world marketplace, and to empower consumers to make purchases that support their values.

10. Fair trade practices include:

- direct trade relationships and long-term contracts between importers and producer groups;
- sourcing from small-farmer or artisan co-operatives;
- higher than conventional market prices, either through above-market premiums and/or price floors;
- provision of affordable credit;
- adherence to the policies of the International Labour Organization, particularly those concerning child and forced labour and the right to collective bargaining; and
- prohibition of the use of dangerous pesticides and herbicides and awarding substantial price premiums for the production of certified organic crops.

**FAIR TRADE GOODS**

11. Fair trade is currently working in about 58 developing countries, with the following goods sold under the fair trade system in the following countries: **Coffee**: Cameroon, Colombia, Costa Rica, Dominican Republic, Guatemala, Haiti, Indonesia, Mexico, Nicaragua, Papua New Guinea, Peru, Rwanda, Tanzania and Uganda; **Cocoa**: Belize, Bolivia, Dominican Republic and Ghana; **Fresh Fruit and Juices**: Brazil, Colombia, Costa Rica, Cuba, Dominican Republic, Ecuador, Ghana, South Africa and Windward Islands; **Wine**: South Africa and Chile; **Honey:** Chile, Mexico and Uruguay; **Tea**: India, Kenya, Sri Lanka, Tanzania and Uganda; **Sugar**: Malawi and Paraguay; **Vegetables**: Egypt; **Rice**: India; **Roses**: Kenya; and **Footballs**: Pakistan.

**BENEFITS OF FAIR TRADE**

12. Several independent studies have been undertaken to measure the impact of fair trade on disadvantaged farmers and workers. In 2007, Daniel Jaffee reported on a four-year study of the impact of fair trade on a cooperative of coffee producers in Oaxaca, Mexico. Entitled *Brewing Justice: Fair Trade Coffee, Sustainability, and Survival*, the report found that fair trade paid higher prices to farmers, which increased their household income. Participation in fair trade reduced household debt and enhanced people's economic options.

13. A large and growing body of impact research has given the following as the long-term value to producers in association with fair trade:

- higher returns and stable incomes;
- investing the fair trade premium in strengthening businesses and social assets (health, education and infrastructure);

- access to credit and pre-finance;
- long-term contracts and trading relationships;
- improved terms and conditions for workers;
- increased empowerment; and
- enhanced environmental management.

14. Fair trade also benefits consumers in places such as the United States and Europe by:

- educating consumers about the lives of people who produce the goods;
- offering good-quality food products;
- sharing as much information as possible with consumers; and
- inviting consumers to participate in political activities that seek to improve the lives of farmers.

**SUPPORTING FAIR TRADE**

15. Given the fact that fair trade schemes are essentially voluntary, private-sector initiatives that develop with society and consumer awareness and demand for products produced by small-scale producers and workers, it is necessary for both developed and developing countries to put in place coherent policy frameworks and sufficient support mechanisms for fair trade. The support include among others:

- undertaking studies on the impact of fair trade and the obstacles poor producers encounter;
- supporting the provision of information to consumers of fair trade products; and
- providing finance, technical support and capacity-building to producers and supporting fair trade organizations.

**AGRICULTURAL SUBSIDIES**

16. In order to boost small agricultural producers, it is essential to streamline the implementation of agricultural subsidies. The United Nations Economic Commission for Africa, in a publication entitled *Agricultural Input Business Development in Africa: Opportunities, Issues and Challenges* (2009), reported that "since input subsidies were not effectively reaching the poorest households in the first place, their removal also did not have any effect on poverty and rural incomes". These subsidies are now given in the form of seed and fertilizer packs (Zambia and Malawi) directly to poor households. However, abnormal subsidies granted by developed countries to their farmers tend to disadvantage unsubsidized produce from farmers in developing countries on international markets, as produce from developing countries tend to cost more.

**SUSTAINABLE DEVELOPMENT: THE CHALLENGE**

17. According to the MDG Report 2011, in 2010, net aid disbursements amounted to US$ 128.7 billion, equivalent to 0.32 per cent of developed countries' combined national income. This was the highest level of real aid ever recorded and an increase of 6.5 per cent in real terms over 2009. Aid to developing countries is at a record high but falls short of promises made at G8, G20 and other donor forums. Compliance by developed countries with their commitments, including an ODA level of 0.7 per cent of GNI by 2015, and compliance with the principles of aid effectiveness are critical. But this will not be sufficient.

18. Compounding the challenge, the global financial crisis and recession and the resulting fiscal consolidations, have seriously undermined governments' ability to meet their pre-existing commitments. The recent sovereign debt crisis in Europe has only served to underline the severe fiscal pressure which is continuing to be placed on many countries.

19. The UN Department of Economic and Social Affairs estimates the annual incremental investment requirements for achieving sustainable development objectives across a number of key sectors at about 3 per cent of gross world product up to 2050 (equal to over US$ 1.9 trillion in 2010). Much of the incremental investment in green technology will need to take place in developing countries. Assuming a share of 60 per cent of global investment is needed for developing countries, at least US$ 1.1 trillion will be needed per year for incremental investments in green technology in developing countries.

## SOME INNOVATIVE FINANCING MECHANISMS (OECD-DAC, 2009)

20. The first innovative financing mechanisms were created to combine public and private contributions to meet major health challenges. These were the GAVI Alliance (formerly known as the Global Alliance for Vaccines and Immunization) and the Global Fund to Fight AIDS, Tuberculosis and Malaria. Each took advantage of the upsurge in private philanthropy for development, particularly through the Bill and Melinda Gates Foundation, to create a new type of public-private partnership that would fund major disease-fighting campaigns in developing countries.

21. These new health sector funds have themselves become drivers of further innovation. GAVI is now largely funded through the International Finance Facility for Immunization (IFFIm), which is expected to raise a total of US$ 4 billion by issuing bonds against long-term ODA commitments from eight donor countries. Through this mechanism, governments contribute to IFFIm to meet interest payments and the ultimate redemption of the bonds. Meanwhile, the Global Fund is now receiving contributions from (PRODUCT) RED, to which credit card and other companies contribute a share of their profits on goods marked with the (PRODUCT) RED trademark. The Global Fund has also made use of a more traditional form of development assistance – debt relief – through the Debt2Health initiative, by which donors forgive the debt owned by developing countries on condition that these countries contribute half the forgiven amounts to Global Fund programmes there.

22. The financial crisis has also sharpened interest in schemes that involve a small levy on private (or sometimes public) purchases. The air ticket levy scheme launched in 2006 had, by 2009, been adopted by 13 countries, and an international purchase facility, UNITAID, has been created to distribute its proceeds with the objective of scaling up access to treatments for AIDS, tuberculosis and malaria.

23. The use of guarantees and insurance to stimulate financing for development is also expanding. In June 2009, the first Advance Market Commitment (AMC) was launched for the development of a vaccine against pneumococcal disease. Under this scheme, private and public donors commit to subsidize a vaccine which passes agreed tests. This provides a new incentive to pharmaceutical companies to develop a product that might otherwise not be commercially viable. Another type of financial promise that has recently been suggested is weather insurance. Here donors must put up the funds to buy an insurance policy. If stipulated rainfall or other thresholds are later met, the policy is triggered and farmers receive the indemnity specified in the policy.

**OTHER MECHANISMS**

24. Other schemes may be established soon, and the Leading Group on Innovative Financing for Development has discussed a variety of possible initiatives. These include Mr. Douste-Blazy's proposal for a global voluntary contribution on airline tickets, separate from the levy, and the implementation of the long-standing proposal for a tax on foreign exchange transactions (often referred to as a "Tobin tax" after its original proponent, Nobel economist James Tobin) which is discussed further. This model of voluntary levy has already been applied by the Global Digital Solidarity Fund, to which private or government bodies contribute 1 per cent of the value of new information technology contracts. The scheme was established in 2003 to help bridge the "digital divide" in developing countries. Other potentially successful mechanisms include: measures to increase the net effects of remittances, microtaxes, a world lottery, etc.

**INTERNATIONAL TAXATION**

25. The growth of the global economy has not been matched with effective means to levy global economic activity in order to pay for global public goods. If the global community fails to fund the required mitigation and adaptation measures, we face a shared risk of global economic, financial, social and environmental instability, which would undermine the foundations of globalization. Solving this dilemma is central to addressing the funding gap in a sustainable way, according to the report of the Committee of Experts to the Taskforce on International Financial Transactions and Development (2010).

26. The Committee believes that the financial sector is the most appropriate point to levy such an innovative financing mechanism. The architecture of the sector is intertwined with the globalized economy, is a primary beneficiary of the growth of the global economy, and – with the liberalization of the capital markets – has been pivotal to the development of the global economy. As such, the financial sector is uniquely placed as a channel to redistribute some of the wealth of globalization towards the provision of global public goods.

27. The Committee concludes that a global currency transaction tax (CTT), which would apply to foreign exchange transactions on all major currency-markets at point of global settlement, would be the best solution.

28. The Committee estimates the total annual foreign exchange turnover (2009) at US$ 909.392 billion (daily total: US$ 3.637 billion). A global 0,005 per cent transaction tax levied on all four major currencies (dollar, sterling, euro and yen) would yield US$ 33.47 billion annually.

29. Nevertheless, it should be clear that ODA alone will fail to eradicate poverty if donors do not take a resolute stance against corruption by their own economic operators and corrupt administrations in recipient countries. Therefore, it is necessary to enhance assistance in the area of strengthening the tax authorities, the judiciary and anti-corruption agencies in developing countries as well as combating bribery committed by companies which are domiciled in the jurisdictions of donor countries, but which have operations in developing countries. An estimated € 800 billion, i.e. almost 10 times the amount of ODA, is lost annually from developing countries through illicit practices such as unlawful capital flows and tax evasion, the prevention and reduction of which could prove decisive in achieving the MDGs. The fight against tax havens, corruption and harmful tax structures should be placed at the top of the agenda in all international forums so as to enable developing countries to increase their domestic revenue.

30. In addition, the introduction of innovative financing mechanisms cannot be a substitute for the full implementation of the Monterrey Consensus and Doha Declaration on Financing for Development. In particular, given the growing importance of remittances, greater efforts need to be made by both receiving and sending countries to tap the economic potential of diasporas, including by providing an enabling legal, regulatory and institutional environment and reducing remittance costs.

**CLIMATE FINANCE**

31. Climate change will affect developing countries in particular and funding measures to alleviate the effects of climate change and reduce energy poverty will contribute to achieving the MDGs. Developing countries are the least well-equipped to deal with climate change, and are, generally speaking, likely to be the principal victims of this phenomenon.

32. The debate on climate change has to some extent been conducted separately from the one on development. This is a mistake. They are intimately interconnected, especially in the area of adaptation. In addition, there is a real trade-off for poorer countries, which already see their scarce development resources potentially diverted to climate action – despite the rhetoric that climate funding should be new and additional. This is a serious issue for Africa: while the continent contributes less than 4 per cent to global warming, it is already affected by climate change, bearing considerable adaptation costs and attempting to mitigate risk. Studies suggest the economic loss to Africa could be in the order of 1.5-3 per cent of GDP annually by 2030.

33. Since 2004, half a dozen mechanisms have raised US$31 billion; 90 per cent was raised through carbon emission trading which can also be considered "additional" to previously budgeted ODA. The additional resources committed to address the needs of developing countries in the Copenhagen Accord are US$ 100 billion a year by 2020. Estimates of funding requirements vary, but, despite differences in numbers, it is clear that there are shortfalls in the total resources needed for climate change and the environment.

34. In November 2010, the Secretary-General's High-level Advisory Group on Climate Change Financing included financial transaction taxes as one of many options to finance a part of the Copenhagen Accord commitments. According to the Advisory Group, auctions of emissions allowances and new carbon taxes in developed countries have the greatest revenue contribution potential among the new public instruments examined by generating US$ 30 billion annually. Another US$10 billion could be raised annually from taxing carbon emissions from international (maritime and aviation) transportation, and up to US$ 10 billion could be mobilized from some form of financial transaction tax implemented among interested countries at the national or regional level. These numbers indicate that innovative financing mechanisms could finance about one half of the annual commitment of US$100 billion under the Copenhagen Accord.