

Questions & Answers

Cocoa conversion rates for mass balance

19 December 2013

Overview

The Standards Committee has clarified the intention of the Fairtrade Standards regarding mass balance conversion rates for cocoa. Fairtrade will require all operators to adopt one set of conversion rates when determining the bean equivalent of semi-processed cocoa products sold or used in production. These conversion rates reflect the intention of the Standard; that mass balance shall be based on the reality of physical processing yields. Standardizing one set of conversion rates and how they may be applied ensures fairness for all operators, including those applying mass balance and those applying physical traceability. This is compatible with the long term aspiration of Fairtrade to move closer towards physical traceability in the future.

This document is in addition to the announcement of the mass balance conversion rate section (section 2.1) in the cocoa product standard. The intention of this document is to answer stakeholder questions regarding the application of the cocoa conversion rates.

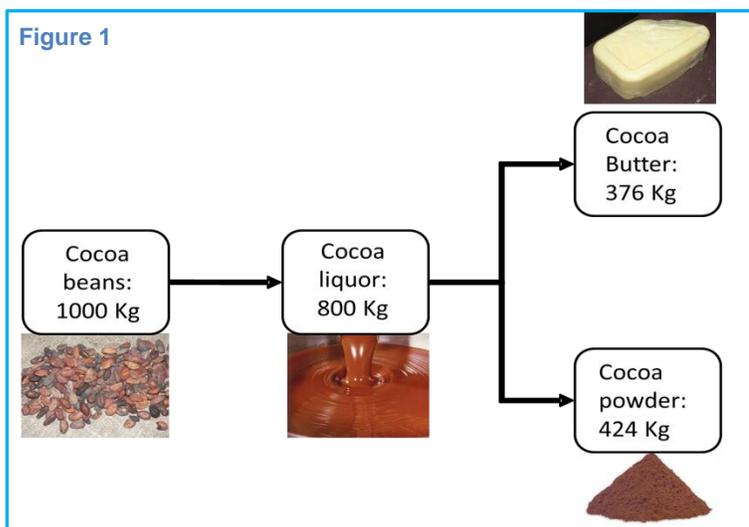
Q & A

Why did Fairtrade decide to publish Fairtrade mass balance conversion rates?

Transparency and fairness are at the heart of Fairtrade. Therefore Fairtrade considers it important that all operators are informed of the conversion rates to be used under mass balance. Moreover, Fairtrade wants to ensure fairness for all operators, whether applying physical traceability or mass balance.

What are the published conversion rates based on?

The published conversion rates are based on physical processing reality, as shown in the diagram opposite. These are the yields quoted in the International Cocoa Agreement (Article 34) and the processing yields currently mentioned in the Fairtrade Standards for pricing of cocoa products sold by Fairtrade producers. Industry adopted norms are also very close to these processing yields, with only minor discrepancies. Therefore Fairtrade considers that these figures represent a fair average.



Why are operators not allowed to apply their actual processing yields / conversion rates to mass balance in Fairtrade?

Fairtrade believes that the transparency and fairness which Fairtrade stands for is best achieved when all operators apply the same set of conversion rates to their mass balance operations.

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When will the announced conversion rates become valid?

The Fairtrade conversion rates will become valid as of 1 January 2014 for all new Fairtrade business (contracts). However, a transition period will apply for the implementation of the Fairtrade conversion factors for existing Fairtrade business until 30th September 2014.

What is the impact of this decision on Fairtrade producers?

This decision is in the interest of Fairtrade producers, because it ensures that the amount of Fairtrade cocoa beans they sell is based on the amount physically required to produce the Fairtrade liquor, butter and powder used in Fairtrade cocoa products.

Why and to whom does the transition period apply?

As the 2013-2014 cocoa season is well underway (the season runs from 1 October to 30 September), Fairtrade appreciates that many operators have already signed Fairtrade contracts and made financial plans for this season. Although all operators are encouraged to apply the Fairtrade conversion as soon as possible, the Standards Committee acknowledged that it could be too disruptive for operators to start applying the Fairtrade conversion rates as of 1st January 2014. Therefore, the Standards Committee agreed to a transition period for existing Fairtrade business. All new Fairtrade business, under the all-that-can-be (ATCB) and Fairtrade Sourcing Program model, will be required to implement the Fairtrade conversion rates as of 1st January 2014. For new Fairtrade business no transition period will apply. This means that existing operators who sign contracts for new Fairtrade business after 1 January 2014 have the choice to:

1. immediately apply the Fairtrade conversion rates to all of their Fairtrade business in 2014
2. implement a dual system in 2014, in which they apply the Fairtrade conversion rates to new business and continue to apply their existing rates to existing business until latest 30th September 2014.

Why did Fairtrade not conduct a public consultation on mass balance conversion rates?

The Generic Fairtrade Trade Standard stipulates that the amount of outputs sold as Fairtrade must be equivalent to the amount of inputs sourced as Fairtrade taking into account the processing yields and all losses (Trade Standard requirement 2.1.8). It also states that Fairtrade inputs shall be of the same kind and quality as the inputs used to process the Fairtrade output ("like for like", Trade Standard requirement 2.1.11). The Standards Committee acknowledged that this is only compatible with processing yields which are based on physical reality. The decision to adopt one set of conversion rates, which are based on physical processing yields, therefore only represents a clarification of the intention of the Fairtrade Standard. The Standards Committee explicitly endorsed the process followed by Fairtrade International for the mass balance conversion factor project and the fact that a clarification of the intention of the existing Standard does not require a public consultation.

Why can a lower conversion rate be used if both butter and powder are sold or used in production during the same time period?

The conversion rates convert semi-processed products back to bean equivalents. As shown in figure 1, from 1 MT of Fairtrade beans 376 kg of Fairtrade butter and 424 kg of Fairtrade powder can be produced at the same time. The amount of beans needed to produce 376 Kg of butter **and** 424 kg of powder is therefore the same as the amount of beans needed to produce 376 Kg of butter **or** 424 kg of powder.

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When selling/using both Fairtrade butter and the Fairtrade powder, the average conversion rate back to beans can be lower ($1.25 = 1000 / 800$) than when selling/using in production only one of these semi-processed products.

When selling Fairtrade butter without the Fairtrade powder, the conversion rate of 2.66 applies: $2.66 = 1000 \text{ Kg of beans} / 376 \text{ Kg of butter}$. Similarly, when selling only Fairtrade powder 2.36 applies: $2.36 = 1000 \text{ Kg of beans} / 424 \text{ Kg of powder}$.

Why can butter and powder volumes be considered together?

In mass balance it is not possible to link semi-processed products sold or used in production to physical processing. Since the actual simultaneous processing cannot be used as a basis, Fairtrade decided to determine a time period in which butter and powder can be considered as being sold / used in production together.

The physical reality is that from 1MT of beans you can at the same time produce 376 Kg of butter and 424 Kg of powder. If mass balance operators were never allowed to consider butter and powder together, they would be disadvantaged compared to operators applying physical traceability and using both Fairtrade butter and Fairtrade powder. An internal consultation with key stakeholders revealed that a period of 12 months was considered most fair to all operators. It is also important to realize that operators applying physical traceability can store Fairtrade butter and Fairtrade powder (derived from one lot of beans) before selling it. Physically traceable operators can thus also sell Fairtrade cocoa butter and Fairtrade cocoa powder at separate moments in time.

Why can companies determine the period in which butter and powder can be considered together?

Fairtrade acknowledges that different companies have different fiscal years and different audit schedules. Many Fairtrade cocoa operators do not base their reporting on a calendar year. Giving each operator the flexibility to determine the period in which Fairtrade butter and Fairtrade powder sales/usage in production) can be considered together ensures that all companies can benefit from a 12 month period that is most in line with their usual reporting schedule. This limits any additional reporting requirements for operators. It also gives companies the option to consider a shorter time period or even not to consider Fairtrade butter and Fairtrade powder together (and in all cases apply the higher conversion rates) if they so choose.

Why does Fairtrade allow operators to apply the higher conversion rate to the major product (of butter and powder) and not count the minor product (see guidance in the Standard)?

Companies typically know if they will sell/use more Fairtrade butter or Fairtrade powder at the beginning of a period. They may however not know the precise volumes. It is therefore easier to always apply the higher conversion factor to the major product (the product most sold/used) and not count the minor product (the product least sold/used) during a period of up to 12 months. Mathematically this is exactly the same as using the lower factors for volumes that can be considered together using the Fairtrade processing ratio of 100:113.

Note that because of this processing ratio operators need 13% more Fairtrade powder than Fairtrade butter to consider powder the major product. This is because 13% more powder (424 Kg) than butter (376 Kg) is produced from 1MT of beans.

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How does this decision impact Fairtrade operators applying physical traceability (including those dealing in organic cocoa)?

This decision helps to ensure fairness for all operators, including those applying physical traceability, because the Fairtrade conversion rates are based on physical reality. Therefore those operators applying physical traceability will not be unfairly disadvantaged.

Why does Fairtrade allow mass balance at all?

Fairtrade's long term aspiration for cocoa is to move closer towards physical traceability in the future. At the moment this is challenging due to the scale at which processing takes place compared to the relatively low volumes of Fairtrade certified cocoa being processed. The conversion rates decision of the Standards Committee underlines Fairtrade's commitment to ensure greater fairness for physical traceable chains and the commitment to move closer towards physical traceability in Fairtrade cocoa.

What is the impact of these conversion rates on operators that only sell/use in production Fairtrade butter or Fairtrade powder?

The conversion rates that apply to each operator are based on how balanced their Fairtrade butter and Fairtrade powder sales/usage actually are. Operators' conversion rates will be by influenced by their demand for both Fairtrade butter and Fairtrade powder.

The conversion rates are also of particular importance for the allocation of the Fairtrade Premium to Fairtrade semi-processed products further up the supply chain. When operators sell both Fairtrade butter and Fairtrade powder, it is possible to allocate Fairtrade Premium costs to both products. This means that buyers of Fairtrade butter and powder can benefit from the balance achieved by these suppliers, rather than having to cover the entire cost of the Fairtrade Premium (\$200 USD per MT) on one product alone e.g. Fairtrade butter.

Why are mass balance conversions only allowed in the direction of processing (e.g. from bean to semi-processed products and not vice-versa)?

Fairtrade's objective is that mass balance remains as close to physical processing reality as possible, for the sake of fair competition between operators, and because it is what consumers expect. 1 MT of beans can be converted into liquor (800 Kg). 800 Kg of liquor can be converted into 376 Kg of butter and 424 Kg of powder. This means that Fairtrade does not allow powder to be interchanged with butter under mass balance and vice versa. The aim of this is, again, to ensure fairness for all operators and that physical traceability remains competitive.

How can I receive additional information concerning the Standards Unit decision for mass balance conversion rates and support on implementing the Fairtrade conversion rates?

Fairtrade is glad to answer your questions and to support Fairtrade certified mass balance operators to implement the Fairtrade conversion rates. For more information on this, please contact Standards & Pricing via email: standards-pricing@fairtrade.net