IMPACT CREDITS
(in the context of Responsible Leather)

DRAFT ONLY
Introduction

The following draft set of slides have been put together to provide a deeper explanation of the what, why and how of Impact Credits. There are many further layers of information and application for the credits, but I have put them together on the context of leather to show how they can work.

Please note that we are still in the process of developing the concepts and systems behind the Impact Credits, working closely with the GRSB, Proterra and Lieven Callewaert.

We want everyone to clearly understand and ultimately support Impact Credits, so please send any feedback to anne@textileexchange.org. Your suggestions on the content and presentation will be highly valued!
What are Impact Credits?
What are Impact Credits?

Impact Credits refer to the certificates that are traded in support of a sustainability claim. The credits are issued when a set of criteria have been confirmed to have been met. The physical goods and the credits are traded separately from each other. The credit certificates represent a specified quantity of verified material that has been produced but has not been physically traded as verified goods.

The way they work is quite simple; farms that meet the standard or benchmark will be able to sell credits for their volume of output, and brands can purchase these credits to balance out their use of these output materials. The farms selling the credits may or may not be in the supply chain of the brands, as the credit trading system does not address any traceability. While this means that brands cannot make any content claims on their products, they can by-pass the cost and complexity of long or opaque supply chains in order to deliver impact quickly and efficiently. And they can still make claims about their support for best practices.

*Impact Credits are essentially a mechanism for brands to deliver their expectations back to the start of the supply chain and provide financial rewards to incentivize them.*
Credit bypass the supply chain...

Possible ownership by traders
Why Impact Credits?
Why Impact Credits?

The idea for Impact Credits came about when Textile Exchange was asked to develop a solution for brands to address animal welfare in their leather supply chains. When we looked at the leather supply chain, however, we realized that it is almost impossible to offer a traceability solution:

- There is little integration between the cattle, hide and leather sectors
- Hides often treated as a commodity product and traded globally
- There are numerous stages and changes of ownership as the hides are processed into finished leather
- Hide identity is not preserved at the slaughter stage: even if it is theoretically possible, it is rarely done
- Traceability does not occur between farming stages in many countries
- Hides represent little or no value to the farmer, so as leather users, we have very little influence with the cattle industry
A long, often opaque, supply chain…
1.7 billion cows on 140 million farms

Countries where leather is theoretically traceably to direct farms.*

Countries where leather is theoretically traceably to birth farms.*

*According to Leather Working Group research
We needed a powerful solution

We decided to bypass the cost and complexity of tracking cattle and hides along the supply chain, and to instead invest in credit trading as the main tool for brands to signal their expectations and support of best practices at the start of their supply chains. This approach offers a number of important advantages:

**Fast**
- The thinking and technology to support credit trading already exists; we are simply applying it to a new commodity.
- We can avoid the time it would take for brands to map their supply chains and find ways to trace materials.

**Efficient**
- Rather than paying farmers a premium for best practices, then having every stage along the supply chain add their margin to that premium, the end buyers (brands or retailers) can transfer their support directly to the farmers, with just a small fee paid for the transfer of the credits.

**Flexible**
- Credits can be used across multiple commodities that have overlapping supply chains and/or impacts (e.g.: leather and beef are linked to cattle, cattle and soy both have impacts on deforestation)
Theories of Change
### Strategy

Use market forces to encourage and support farmers to meet a minimum level of best practices.

### How

Develop credits as a means for brands and retailers to support and incentivize best practices at the start of the supply chain.

**What needs to be true?**
- Credits are adopted at scale
- Credits address the areas of highest concern to brands
- Credits are highly credible: verified and deliver meaningful change
- Credit prices are high enough to incentivize sustained change
- Credits can be easily understood by farmers, brands and consumers (simple messaging)

### Outputs

- Clear criteria and verification requirements that farmers must meet to be able to sell Impact Credits.
- An efficient system to register, sell and redeem credits.
- Clear and credible claims language to support the use of credits.
- Sustained marketing to support the value and scale the adoption of Impact Credits.

### Goal

Widescale recognition and support of best practices at the farm level.

Widescale adoption of best practices across multiple commodities.
How Impacts Work
Credit and payments flow*

Verification Body

Farm or Farm Group

Credit Platform

Facilitator

IMPACT ALLIANCE

Brand

Claims

*Please see notes field for explanation
Roles

Farm, Farm Group or Program Partner: Meet the requirements set out for Responsible Leather (eg: DCF, animal welfare). Agree to be verified by a third party and to submit the requested data.

Verification Body: Act as a credible third party to verify the farm information, and register the credit onto the Credit Trade Platform.

Credit Trade Platform: IT system that holds the registration of credits and the associated data, and records manages the changes of ownership and redemption of credits.

Facilitator: An agent that supports credit buyers to source and purchase impact credits that meet their needs. The facilitator will be paid for their services through the credit price, but cannot engage in any speculative trading.

Brands and Retailers: Companies that are looking to support impact at the start of their supply networks, and invest in developing an increased supply of best-practices materials that they can ultimately link to their product sourcing.

Impact Alliance: A voluntary collaboration of NGOs with common goals, working together to protect and promote the value of Impact Credits.

NGOs: Organizations that are using standards and benchmarks to define and promote best practices.
What goes into a credit for Responsible Leather?

Although the initial demand from brands was to work on Animal Welfare (A/W), we realized that there are other concerns relating to cattle production that we needed to address. While there are numerous important social and environmental issues, we chose to focus on Deforestation and Conversion-Free (DCF). Not only are brands feeling pressure from investors and special interest groups to address deforestation, but we saw an opportunity to have a positive impact on climate change and biodiversity loss.

The other pressure that leather brands are facing is to make their supply chains deforestation-free. However, this is almost impossible in most cases, due to the length and complexity of the supply chain, and the current lack of systems to support traceability of cattle, even in countries like the United States. We therefore decided that to qualify for a credit, farmers must also participate in a traceability scheme. While RFID ear tags would be the ideal solution, we decided it was important to meet farmers where they are at, so will recognize any credible traceability system.

To offer the most flexibility to both farmers and brands, credits can be generated and sold for either animal welfare, deforestation and conversion-free, or both combined.

In all cases, the credits must be verified by a third party before being registered onto the trading platform.
All of these combinations will count as Responsible Leather Credits, and will allow buyers to use credits to meet their specific goals, while allowing farmers to be recognized for their best practices. The expectation is that credits that address multiple scopes (ie: both animal welfare and DCF) will command higher values, but the selling price of the credits will be ultimately determined by supply and demand factors. Over time we may add additional scopes to the Responsible Leather Credits.
For each Impact Scope, the Impact Alliance will set a minimum threshold of best practices to qualify for Impact Credits. The individual NGOs may set higher requirements, but they cannot become part of the Alliance with lower ones. As much as possible, these thresholds will align with internationally accepted definitions and targets.

* Based on Accountability Framework definitions
How are Credits Calculated?

There are some complex equations to calculate credits, but at the simplest level, one cow = one credit = one hide.

While some of impacts may be more related to the area of the farm (eg: deforestation), and others to the number of animals (eg: animal welfare), we have chosen to use the number of cows as the proxy for the number of credits, as it is easy for everyone to understand, and mirrors the physical souring of products.

How do Brands Use Credits?

Basically, brands will use leather credits to ‘balance out’ their use of hides. We could use the terms ‘offset’ or ‘inset’, but these have been met with confusion. So if a brand uses 10,000 hides in a year, they could purchase 10,000 credits, and make a statement such as: “For each hide we use, we ensure that a cow is being raised on a farm that meets the animal welfare and deforestation requirements set by Responsible Leather.”

Or, as farm data is collected, they may be able to say “Though the use of Impact Credits, we are supporting the conservation of 10,000 acres in the Matto Grosso region.”
Impact Partnership Credits
What about marginal farmers that cannot meet a standard?

Standards are a great way to recognize and reward best practices where they are happening, but they are not always the best tool for farmers that need support to make changes that are needed.

Impact Credits can also be sold by programs that are working with farmers to improve practices and meet minimum levels of best practices. They are a tool to help brands work with on-the-ground program partners to support farmers to meet the best practices and set themselves up for credit trading and/or physical trading. The program partners deliver trainings, verification, and collect data with the farmers, while offering stories, data and credibility back to the brands. Although the programs can go on indefinitely, the individual farms will only count for credits for three years, so that we are constantly moving them to improved practices, and making room for new ones to be involved. After three years, or ideally less, the farms can trade credits directly with the brands, and get the money into their own pockets. All of this will drive up the supply of the preferred material, creating that scale of change we need to address the issues facing our planet, as well as the scale of supply that brands can ultimately bring into their supply chains.
Impact Partnership Credits support change through Programs, and Impact Credits sustain it with Farmers.
Impact Credits Partnership: Programs and Farms

- Impact Partnership Credits can also be used to help drive progress towards the benchmark thresholds. Brands will give money to program partners that will then work with producers on capacity building, data collection, verification and trading support.

- Farmers can be supported through Program for up to three years under the Impact Partnership Credit system. After that they can remain in the program, but will not count towards Impact Credits being earned by the program.

- When the farmers meet the standard or benchmark that is set, they can trade credits directly (which is a financial incentive).

- Brands can also make long-term commitments to support specific programs through the Impact Partnership Credits.
Impact Credits or Impact Credits + Impact Partnership Credits

Brands will have multiple options to look at. They can choose a focused strategy for buying credits, or take a portfolio approach.
What about the Beef Industry?

From the beginning we realized that we could not address issues at the farm level on our own. As the textile industry, we have little or no voice with farmers. However, our brands and retailers have a very strong relationship with consumers, and are strongly motivated to meet their CSR goals. We were fortunate early on to connect with the **Global Roundtable for Sustainable Beef**. Through their network of national roundtables, they have a strong voice with farmers and share very similar goals and values with Textile Exchange and Responsible Leather. Together we can combine two powerful industries to achieve the scale and pace of change that is needed to address the world’s most pressing issues.

This is all good news for the farmer when it comes to the credits. They can earn even more rewards by selling credits to both beef and leather buyers.
So Why Call Them “Impact Credits”?

The idea behind calling the credits “Impact Credits” is to recognize that they are credits designed to support positive impact across a range of dimensions and commodities. The name provides the flexibility for the credits to address different scopes of impact and work for different sources of raw materials. The concept works not only for beef and leather, but also cotton and soy. As of November, 2019, we have 3 NGOs representing 4 commodities who are working together to develop the concept of Impact Credits and to create the Impact Alliance. We also have strong interest from another 4 NGOs that are interested in using Impact Credits to support the standards and commodities that they are working with.

The good news is that we are moving forward quickly, thanks to the commitment of two key industry players: ChainPoint and ACT Commodities are enthusiastic partners in developing Impact Credits and supporting the Impact Alliance. They are partnering to co-invest in the development of the trading platform that will be used not only to register and trade credits, but to gather important information and data.
Impact Credits: a tool that works across multiple standards, commodities, markets and farm systems
Impact Credits: a tool that can leverage the connections

There are many cases where Impact Credits can have multiple roles for buyers and/or sellers. Consider a company like Ikea that buys cotton and leather for its furnishings, as well as beef and soy for its food products. Or a farmer that rotates between cotton and soy. That same farmer may even own cattle.
What is the Impact Alliance?

The **Impact Alliance** is a voluntary collaboration between sustainability standards owners that provides oversight on the use of Impact Credits. The purpose of the Alliance is to use Impact Credits to accelerate the positive impacts of sustainability schemes in order to address the key issues facing the future of our planet. We need to **protect and promote the value of Impact Credits**. The first activities of the Impact Alliance first work will be to enter into an agreement with the Credit Trade Platform, define the core principles behind Impact Credits, and set up the rules for the registration and sale of credits.

By working together, we can leverage our separate and shared sources and markets. We can combine our efforts to create more efficient systems, and report out on a much larger impact that we ever could individually. The more that join us, the more powerful we can all be.
Setting up Partnerships

- TextileExchange
- Textile Exchange Responsible Leather Round Table
- GRSB
- ProTerra Foundation
- Others (TBD)

**IMPACT ALLIANCE**

Credit Trade Platform

- ACT
- ChainPoint
Defining Impacts

A critical piece of work for the Impact Alliance will be to determine which baseline criteria must apply across all credits, and what data will be collected to measure the impacts. By working together, we not only protect the integrity and value of Impact claims, but we make it easier for farmers who want to meet the requirements, and increase the value for brands that want to report on progress towards their targets.

For example, if we require that all Impact Credits can only be issued to farms that are Deforestation/Conversion-Free (DCF) (which will apply primarily to cattle and soy production), and encourage brands to purchase from targeted high-risk areas, then we send combined market signals to accelerate the protection of forests where it is needed most. Impact Credits act as the “invisible hand” to align the intentions and actions of brands and retailers from different parts of the food and textile industry. Imagine farmers in the Amazon receiving credits linked to car companies, supermarket chains, fashion brands, restaurant chains and footwear brands!

In addition setting shared minimum requirements, we can set common data to be collected. In the case of beef and leather, for example, that would include information such as:

- Farm location and mapping (polygon)
- Area of land (forest or grassland) being conserved
- Number of animals, etc.

Ultimately, we will want to translate this data to impacts (e.g.: biodiversity, carbon) so that all players can track their progress towards targets and goals.
Individual and Shared Expectations

<table>
<thead>
<tr>
<th>Leather</th>
<th>Beef</th>
<th>Soy</th>
</tr>
</thead>
<tbody>
<tr>
<td>Animal Welfare</td>
<td>Animal Welfare</td>
<td>Non-GMO</td>
</tr>
<tr>
<td>Deforestation/Conversion-Free</td>
<td>Deforestation/Conversion-Free</td>
<td>Deforestation/Conversion-Free</td>
</tr>
<tr>
<td>Traceable</td>
<td>Traceable</td>
<td>Traceable</td>
</tr>
<tr>
<td>Verified</td>
<td>Verified</td>
<td>Verified</td>
</tr>
<tr>
<td>Data</td>
<td>Data</td>
<td>Data</td>
</tr>
</tbody>
</table>

While each NGO can set the criteria that best matches its goals, we will look for the issues that we share, set minimum requirements that all will meet or exceed, and identify core data to collect (to measure impacts.)
Potential Core Areas for Impact Credits

Potential Impact Areas (Scopes)
- Traceability
- Animals
- Water
- People
- Land Use
- Soil Health
- Air
- Waste

Data to be collected
- Farm outputs
- Location (region)
- Total farm area
- Area of forest conserved
- Etc.

Impact Measurements (longer term goal)
- Carbon*
- Biodiversity*
- Etc.

* Align with Science Based Targets

Soy, Beef, Leather, Cotton, Sugar, ...more...

* Align with Science Based Targets
Each NGO sets their own requirements and sells their own credits.

All credits will reference the same definitions and respect a minimum threshold.

- Farm outputs
- Location (region)
- Total farm area
- Area of forest conservation
- Etc.

Common data points will be collected across all credits.

As the program develops, the data can be converted into specific impact measurements.

Impact data can be combined with external data and reported out. *For specific regions only*
Impact Alliance partners agree to use common definitions and targets. Common principles must be met, but each organization can set its individual requirements.

Commons sets of impact data will be collected across the participating commodities. Data will be collected through the Credit Trade platform then could be transferred to a broader reporting system.

We can match KPIs to the ones used by the SBTi. **Note that Impact Credits cannot be used for brand progress to SBTs. We will need to talk with SBTi about how to talk about impacts that are not directly linked to sourcing.

Credit buyers and the Impact Alliance can talk credibly about the actions they are taking to support the Sustainable Development Goals.
Credit Buying Strategies
Brands will have multiple sourcing models to work with:

- Physical Trading
- Impact Credits
- Impact Partnership Credits
Brands have a path towards full traceability:

- **2025**: 50% of leather sourced from fully traceable Responsible Leather supply chains.
- **2030**: 50% of leather use offset with Responsible Leather Impact Credits or Impact Partnerships.
- **2040**: 100% of leather sourced from fully traceable Responsible Leather supply chains.

100% of leather use offset with Responsible Leather Impact Credits or Impact Partnerships.
Brands can use different strategies:

- Buy credits to match sourcing regions
- Buy credits to meet impact targets
- Combination
Decoupling Impact Credits from Physical Supply

Brands and retailers can choose different strategies for working with Impact Credits.

**Impact Credits to Match Sourcing**
Some companies may choose to buy credits from the regions they source from. For example, if a footwear brand sources half of its leather from the U.S. and half from Europe, they may choose to buy 50% of their credits from American farmers and 50% from European farmers. However, the reality is that most brands do not know which countries their leather comes from, so this is not even an option for them.

**Impact Credits to Reach Goals**
Another strategy is to source credits from the areas of highest risk, in order to deliver support for best practices where it is needed most. Even if a brand knows its supply chains, this may be a more powerful option for them. For example, if a footwear brand is being attacked by special interest groups for sourcing from Brazil, they may choose to source their physical leather from “safe” countries, but still purchase DCF credits from farms in the Amazon to support the preservation of forests.

**Amplifying the Potential for Impact**
Through the Impact Alliance we can take this even further: if we all encourage the brands and retailers who purchase Impact Credits to focus on a specific region, we can concentrate a significant amount of financial support for forest protection in a high-risk area, and everyone will benefit by telling a stronger story of the combined impact. Impact Credits can contribute to a broader sectoral agreement: they become a common language and currency across geographies and markets.
Strategy
Match credit purchases to physical sourcing

- Impact Credit Sourcing
- Leather Sourcing
Strategy
Decouple credit purchases from physical sourcing

- Impact Credit Sourcing
- Leather Sourcing
If multiple brands choose this strategy and align their credit purchases to a high-risk area, there is potential for significant impact!

- Impact Credit Sourcing (Leather)
- Impact Credit Sourcing (Beef)
- Impact Credit Sourcing (Soy)
- Impact Credit Sourcing (Leather)
- Impact Credit Sourcing (Beef)
- Impact Credit Sourcing (Soy)

If multiple brands choose this strategy and align their credit purchases to a high-risk area, there is potential for significant impact!
Impact Credits and Traceability
Can we combine traceability and credits?

Yes! In fact, Textile Exchange is looking at this model for cotton. There are a number of brands that would like to use Impact Credits to deliver premiums directly to farmers that are making the transition from conventional to organic practices. The transitional cotton from these farms will enter the supply chains of the brands, but it will be sold at conventional prices and brands will also track the cotton through their supply chains.
Can we still aim for Deforestation-Free Supply Chains?

Yes. But it will take time. In the context of Responsible Leather, we are working from two directions. We are using Impact Credits to require traceability at the farm level, and we require brands that want to say that they are part of the Responsible Leather Program to trace back along their supply chain one step further each year. Within a few years, we should have a good number of brands that can trace back to the slaughterhouse, and a large supply of traceable cattle. During that time, industry effort to develop efficient and effective tracking mechanisms will continue.
Driving to Success
How will Impact Credits Succeed?

• High volume of demand, meaningful prices and sufficient supply
• Collaboration between Impact Alliance partners and other stakeholders
• Strong systems to support the trading of credits
• Credible requirements and verification
• Clear communications and claims guidance

All of these factors are critical to the success of the credits, and we need to support to ensure that they are all met.

Questions?

There are many further levels of detail behind the Impact Credit system, and we are still working on figuring it all out.

If you would like to learn more, or be part of the process, please contact Anne@TextileExchange.org.
Thank you