



Briefing on the Agribusiness Enabling Environment



AgCLIR LESSONS FROM THE FIELD: DEALING WITH LICENSES



The business of agriculture occupies a critical space in most economies. Distinct and special among industries, agriculture is the dominant source of employment for a large share, even a majority, of the population in developing nations.

Accordingly, governments treat the regulation of agriculture and food differently than any other sector. Unlike the output of other sectors, many agricultural products are basic necessities: agriculture provides the food, fiber, fuel, and construction materials necessary to sustain human existence. Governments everywhere assume responsibility for assuring that the distribution of agricultural commodities is great enough and equitable enough to provide a reasonable quality of life for its citizens.

Agriculture and Agribusiness: Dealing with Licenses is a briefer that mirrors the analytical framework used by the World Bank Group's Doing Business series (www.doingbusiness.com) and adopted by USAID's Business Climate Legal and Institutional Reform Project (www.bizclir.com). Divided into four sections (Legal Framework, Implementing Institutions, Supporting Institutions, and Social Dynamics), this briefer highlights the specific issues that must be addressed in local legal, regulatory, and institutional environments if agribusiness is to be economically productive, contribute to environmental sustainability, and assure a safe and reliable food supply.

DEALING WITH LICENSES: KEY CONCEPTS

The business of agriculture is typically heavily regulated. Moreover, it is often regulated in a way that requires business owners to actively search out what can seem like, under the best of circumstances, inconsistent and counterintuitive licensing requirements. Operating licenses enable governments to control where, how, and under what circumstances businesses may operate. But the licensing process is generally disaggregated, with different licenses and permits required for specific activities and the authority to issue such licenses and permits delegated to a wide range of administrative units in different locations.

Licensing is a common way to regulate activity in all fields. It permits the authorities to track activity, monitor compliance with rules, and acquire promises that licensees will behave in certain ways. The fees collected permit the licensing bodies to remain self-sufficient.

Examples of the kinds of activities that are typically monitored and regulated through licensing include:

- the initial establishment of an agribusiness so that authorities can influence land use according to policy;
- the establishment of quality standards for both processes and products;
- the limitation of environmental damage by requiring licensing for various emissions (e.g., smoke, water, other effluents) that a business may produce;
- the use of certain chemicals to monitor and limit dangers to the environment as well as the consuming public;
- the services sometimes outsourced by agribusiness (such as pesticide spraying and harvesting); and
- the export and import of product and inputs.

A licensing regime must be efficient, fair, transparent, and predictable or it will impede agribusinesses' ability to contribute to growth. An inefficient licensing regime can lead to wholesale avoidance of protocol and to corruption and cheating.

Bureaucratic impediments to licensing stop or slow business investment and growth and reduce competition. Excessively high licenses fees can encourage the operation of illegal businesses and/or environmentally damaging pollution.

Agribusinesses of all sizes generally have to deal with licenses or permits at some point, although the importance of the licensing process is typically more important, and more complicated, for larger and more complex agribusinesses. As in any sector, agribusinesses need permits to construct warehouses and stores, access water and electricity, operate transport vehicles, acquire certification of quality standards for their products, or receive certification for their environmental management procedures.¹

Licensing regimes more specific to the agricultural sector are also common, especially because of the important public health and environmental safety issues associated with agriculture. Agricultural traders are sometimes licensed to trade in certain areas or in certain commodities, with the license based upon their demonstrated knowledge of that commodity or market. Distributors of agricultural inputs (e.g., fertilizers, seeds, herbicides, pesticides) often need to be licensed to deal in such products in the interests of assuring public health and quality control. Food processors are required to be licensed—and are closely overseen to make sure terms of licenses are being fulfilled—for reasons of public health or safety. And virtually all other processors are increasingly subject to licenses or permits aimed at reducing harmful environmental effluents.

While small farmers or animal producers may not need to apply formally for licenses to operate, they are, however, subject indirectly to the licensing regimes that affect other players in the supply chain. For example:

- the improved seeds small farmers buy are often produced under license;
- the products they sell either as individuals or as members of a cooperative may need to be quality or safety certified; and
- their access to transport and other utilities and services may also be subject to licensing and permitting procedures.

LEGAL FRAMEWORK

The responsibility for licensing and permitting is generally widely dispersed among various levels of government: state, regional, and local. In the United States, much of the licensing and certification relevant to agricultural production processes, including input supply, is the responsibility of state governments. Processing raw agricultural materials into food or other products and marketing of these materials, however, tend to be the regulatory domain of higher levels of government. In developing countries, where many inputs are imported and exports are controlled, national governments and financing institutions retain control of a greater range of relevant licensing for agribusiness.

Licensing requirements in a number of service areas as well as those licenses having to do with public health and both food and environmental safety could add up and have a major impact on

the agribusiness environment. Further, licenses to trade in specific products are sometimes limited to a few exporters to assure quality control for nationally identified exports (e.g., coffee from Ethiopia, Kenya, and Tanzania).

Any discussion of a legal framework must acknowledge the key components of “good” law:

- **clarity**—simple enough so that those regulated by it can easily understand it;
- **fairness**—universally applicable (except in cases in which certain populations are treated differently in order to artificially rectify imbalances; and
- **predictability**—written and applied so that those regulated by the law are able to act with knowledge of the legal outcome.

IMPLEMENTING INSTITUTIONS

For the agricultural sector, there are four categories of national or local government institutions likely to play important roles in issuing business licenses and permits affecting the operation and success of agribusinesses:

- those that license the import and distribution of production input supplies (e.g., seeds, fertilizers, chemicals, equipment);
- those that license services essential to local producers and traders (e.g., veterinary services, transport services, telecommunications services, banking);
- those that license or certify production of food, fiber, or fuel products and production processes (e.g., slaughterhouses or packing plants for meat, dairy processing, other food manufacturing, charcoal or ethanol manufacture); and
- those that set and regulate standards for effluents of processing and manufacturing processes in which agricultural inputs are used (e.g., run-off water containing excess amount of nutrients, disposal of untreated waste in manufacturing plants).

For crop producers, for example, the licensing regimes affecting input supplies are critical. If the procedure for approving new and improved seed varieties is excessively long or burdensome, or if transgenic varieties are not patented or licensed for distribution, farmers may not have access to planting materials that could increase their competitiveness. If licenses for the import and/or distribution of pesticides are not given in a timely way, crops could be lost to locusts or other pests.

Institutions in the agricultural sector are likely to be responsible for most, but not all, of these licenses. Most ministries of agriculture have specialized units for assuring plant and animal health (similar to APHIS in the U.S. Department of Agriculture) and for granting certificates for plant variety protection (PVP) to plant breeders, enabling them to market their new varieties. However, ministries of environment and/or natural resources play a role in setting and regulating environmental standards for agribusinesses that supply inputs, especially herbicides and pesticides, that could have persistent effects on the environment or could result in non-point source pollution in areas away from the production site. Post-Cartagena Protocol controversies on the introduction and management of genetically modified organisms (GMOs) have brought environmental and agricultural ministries into some conflict on that particular issue. Ministries of health play some

¹ Construction of a warehouse is, in fact, the test case for the *Doing Business* assessment.

role in establishing standards for food safety, and some governments, like the United States, have established agencies responsible for licensing on food and drug issues.

SUPPORTING INSTITUTIONS

Among the supporting institutions needed for key support to agribusinesses seeking to acquire legally necessary licenses as well as certifications and permits enabling them to participate in specific markets are:

- laboratories and/or third-party inspectors for food safety certification;
- laboratories for pesticide testing and certification;
- facilities that certify the quality of seed and fertilizer; and provide for spot checking at retail market outlets;
- training institutions that provide information on laws regarding licensing and facilitate agribusinesses' understanding of compliance;
- banks and other financial institutions to provide financial guarantees;
- brokers of various sorts, especially regarding import and export procedures; and
- private sector and industry associations (such as chambers of commerce or more specialized business associations).

The lack of business support services has been noted in many developing countries. Organizations or firms specializing in such services could help to cut through the red tape associated with licensing and certification, thus making the process more transparent and fair. Excessive licensing can result in impenetrable bureaucracy and encourages informal or illegal operation. Thus, the oft-heard demands for less rather than more licensing are understandable, perhaps especially in agribusiness where licensing can spiral out of control.

The involvement of outside analysts and advocates can provide important information and leverage in designing fair and effective licensing regimes. The International Livestock Research Institute (ILRI), for example, demonstrated how excessive licensing laws regarding the milk trade can have adverse effects by encouraging producers and traders to skirt the law and, in the process,

provide unsafe products to consumers. Data showed that the government of Kenya's adoption of international standards requiring industrial pasteurization for retail milk was being applied to only 20 percent of milk consumed. Small commercial producers were meeting 80 percent of market demand but encountering serious business problems, including official harassment, as well as providing a product of variable quality and with some health risks. Researchers proposed that training and licensing smallholder milk producers to provide raw milk meeting key hygiene conditions, rather than policing them and punishing them for not meeting the industrial standards, would actually improve milk safety in the country. It was also found that licensing producers and traders using improved milk handling techniques would contribute to a safe food supply.²

The design of alternative licensing systems, such as that proposed for the Kenyan milk business, is complex and requires considerable research. While it may seem sensible simply to adopt international standards, there may be an economic case for a more locally specific solution. Greater examination of the licensing environment for agribusiness in particular would seem to be warranted in countries where agriculture accounts for a significant share of GDP and exports.

SOCIAL DYNAMICS

No one in the world likes "red tape." It is a result not of design, but of the type of inefficiency and lack of capacity so often found in developing countries. This creates a vicious circle: the more difficult the licensing process, the greater the incentives for avoidance and "informal" operation and, ultimately, a breakdown in the government's ability to address necessary regulatory issues. Further, governmental corruption feeds on its own inability to efficiently regulate. In other words, inefficient government breeds business that avoids official procedures, which in turn creates a market for corruption. As the Kenya example shows, this can have significant negative impacts on public health and safety. In order for growth to be achieved, all components of society need to at least recognize the value of a licensing framework balanced against the legitimate interests of businesses to minimize time spent trying to comply with the law.

2 Overseas Development Institute (ODI) "Bridging the Regulatory Gap for Small-scale Milk Traders," Document Summary, Research and Policy in Development, available at http://www.ilri.org/ilri/pubaware/Uploaded%20Files/200481194330.03BR_ISS_BridgingTheRegulatoryGapForSmallscaleMilkTraders.html

About AgCLIR:

AgCLIR is a unique agribusiness enabling environment diagnostic that provides a comprehensive method to diagnose the root causes and inefficiencies of an underperforming agricultural sector. AgCLIR is one of a series of sector specific diagnostics produced under the USAID BizCLIR project. BizCLIR, or the Business Climate Legal & Institutional Reform Project, is a multi-year initiative of the United States Agency for International Development (USAID) with the goal of improving the business enabling environments through sound analysis and strategic interventions. This series, Briefings on the Agribusiness Enabling Environment is intended to shed light on some of the most important, and least understood, components at the intersection of agribusiness and commercial law and institutional reform. All issues are available at www.bizclir.com.

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