

# Cocoa Coalition joint position paper

## The proposed EU Corporate Sustainability Due Diligence Directive

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The signatories to this position paper welcome the publication of the proposed EU Directive on Corporate Sustainability Due Diligence (COM(2022)71). We believe that the proposed Directive, alongside the proposed Regulation on Deforestation published in November 2021, represents an important step forward in driving the necessary transformation of the cocoa and chocolate sector, among many other areas of activity. We called for legislation for both these approaches to due diligence in the first position paper [we published in 2019](#), and in our more detailed position paper [published in October 2021](#).

We welcome in particular the detailed description in the Directive of the steps companies are to take in implementing their due diligence obligations, including in Articles 7 (Preventing potential adverse impacts) and 8 (Bringing actual adverse impacts to an end). We also welcome the many references to the need for support for SMEs affected by the Directive (which should encompass SMEs outside the EU as well as inside), and provisions to enable access to effective remedy, including civil liability, particularly as no such proposals were included in the Deforestation Regulation.

With regard to cocoa, we have consistently argued that the effectiveness of due diligence legislation will be limited unless it is coupled with action to address the root causes of human rights abuses and environmental harms in cocoa producer countries and to create the enabling environment required to support the transition to sustainable cocoa farming. We are pleased to see in the Directive a recognition of the need for the European Commission and member states to 'continue to work in partnership with third countries' (Recital 49); we consider this in more detail below.

We also note the reference (also in Recital 49) to the need to pay specific attention to 'the challenges faced by smallholders'. This is particularly acute in the cocoa sector, where the vast majority of producers are smallholders, and underlines yet again the need for the Commission and member states to support an enabling environment in producer countries.

We also welcome the provision, in Article 13, for the Commission to issue sector- or impact-specific guidelines. We hope these will be produced by the time the Directive enters into force; we discuss this further below.

We believe that the Directive could be further strengthened in a number of important respects, through the steps outlined below. (This paper sets out the principles of our approach; in due course we intend to propose specific amendments.)

## 1 Partnership agreements in the cocoa sector

We have consistently argued that the effectiveness of due diligence legislation will be limited in the cocoa sector (and almost certainly in other sectors as well) unless it is coupled with the creation of the enabling environment required to address the root causes of human rights abuses, such as the worst forms of child labour, and environmental harms, such as deforestation, both driven by the underlying causes including farmer poverty and slow rural development, and to make progress on sustainable cocoa farming within cocoa-producing countries.

We are therefore pleased to see a recognition of the need for the Commission and member states to ‘continue to work in partnership with third countries’ (Recital 49) but this is not reflected in the text of the Directive and should be referred to explicitly in Article 14(3). (The guidelines on accompanying measures published by the Commission and the International Trade Centre in April 2022 is also welcome.)

Accordingly, we believe that it is essential for the EU to pursue the establishment of long-term partnership agreements with the governments of cocoa-producing countries, ensuring that all relevant stakeholders are involved, including local community representatives, farmers, industry, and civil society. The objectives of these partnership agreements should be to:

- Clarify what is needed to establish a sustainable cocoa sector within the producer-country partner – e.g. improved supply management, development of alternative activities for farmers, sustainable diversification, etc. – and what different actors in the supply chain need to do to achieve it.
- Set out the changes in governance, including transparency, and policy, and/or improved enforcement of existing policies, that would be needed to produce cocoa sustainably.
- Put in place incentive and support mechanisms, including funding, to ensure that the required policy changes and measures are implemented.
- Establish monitoring systems to assess the impacts of the policy changes and measures and ensure that any unintended negative consequences for people or the environment are avoided.

We set out our proposals at more detail in our [paper of June 2021](#). We welcome the announcement, in June 2022, of the ‘Alliance for Sustainable Cocoa’ between the EU and cocoa-producing countries and look forward to playing our part in the implementation of its roadmap for action.

## 2 The due diligence process and business relationships

Although the proposed Directive builds on the approach set out in the UN Guiding Principles on Business and Human Rights and the OECD Due Diligence Guidance for Responsible Business Conduct, it diverges from them in important respects. For us, this is its main weakness.

Both the UN Guiding Principles and the OECD Due Diligence Guidance stress the need for due diligence to be risk-based, for companies to identify, prevent, mitigate and account for how they address their adverse human rights impacts in their operations and supply chains, prioritising the most salient issues. However, this emphasis on risk is largely absent from the proposed Directive, which focuses instead on business contractual relationships.

On top of this, the Directive restricts the due diligence obligations to entities with whom a company has an ‘established business relationship’ (alongside the company’s own operations and subsidiaries) – a term which is difficult to define precisely and does not feature in the UN Guiding Principles or OECD Due Diligence Guidance. This unduly restricts the reach and impact of the due diligence process. In practice, it is entities in more remote parts of the value chain and with whom companies have less well-established business relationships that are often most likely to be associated with adverse human rights and environmental impacts.

In the cocoa sector, this approach risks excluding much of the indirect supply chain (cocoa sourced from local traders as part of origin government regulatory and licensing requirements) as well as the short-term contractual relationships from due diligence obligations, thereby creating an incentive for companies subject to the Directive to change their purchasing practices to circumvent the requirements of the Directive and favour short-term contracts – the opposite of what is needed, since traceability to the source of cocoa beans is far more difficult in these business relationships. In practice, the legislation needs to encourage the establishment of closer and more long-term relationships between companies and their suppliers, including the provision of investment and capacity-building, but it will not do this if part of the supply chain is excluded from the obligations.

We therefore believe that the restriction to ‘established business relationships’ should either be removed or reworded to make it clear that companies are obliged to conduct due diligence across their entire supply chain. Instead, the Directive should be consistent with the UN Guiding Principles, which encourage companies to take a risk-based approach and prioritise their efforts on the basis of: (1) the severity of the actual or potential harm to people and the environment; and (2) the extent of companies’ leverage over their suppliers.

Accordingly, and in line with the UN Guiding Principles, companies should be expected to take appropriate action to identify, prevent, mitigate and account for their adverse human rights and environmental impacts depending on their involvement and the extent of their leverage on their suppliers:

- If a company has caused or may cause an adverse impact, it should cease, prevent or mitigate the impact and remediate any harm if the impact has occurred.
- If a company has contributed or may contribute to an adverse impact, it should cease, prevent or mitigate its own contribution to the impact, and use or increase its leverage with other parties to prevent or mitigate it. It should also contribute to remediating the harm if the impact has occurred, to the extent of its contribution.

- If a company has not caused or contributed to an adverse impact, but its operations, products or services may be linked to an impact through a business relationship, it should use or increase its leverage with other parties, including suppliers, to seek to prevent or mitigate the impact.

These steps may include the option of disengagement from suppliers, but this should always be as a last resort after other measures have been tried and failed. This issue is well covered in Recital 36 of the Directive, but the discussion there is not reflected in the description of the due diligence process in Articles 7 and 8, and these should be amended accordingly. The extent to which disengagement is feasible or legally possible will vary by sector, so the topic should also be covered in more detail in sector-specific guidelines (see Section 9).

Finally, there are also references in Articles 7 and 8 to encouragement for companies to make necessary investments. We agree that this is a valuable measure which should be encouraged, but the references in both articles is to investment in management or production processes and infrastructure – i.e. in processes – and not, as it should be, in prevention, mitigation and remediation activities, where appropriate conducted jointly with other enterprises in the supply chain.

### 3 Purchasing practices

Companies' purchasing practices are critical elements in mitigating against the risk of human rights abuses and environmental harms. This is particularly the case in agricultural supply chains where farmer poverty is prevalent, including cocoa, where purchasing models, alongside other interventions to improve farming profitability, can contribute to achieving living incomes (see Section 4).

We believe that the Directive should incentivise companies regularly to review their purchasing models, with the aim of encouraging the inclusion of social and environmental externalities in the contracts and closing the gap to living income. This can enable the development of closer relationships between buyers and suppliers, encouraging them to work together and facilitating the provision of support and capacity-building in order to create sustainable supply chains, increase farmer incomes and deliver improvements in human rights and environmental outcomes.

In the proposed Directive, the issue of procurement, purchasing and pricing is touched on in Recitals 28 and 30, which raise the idea of a code of conduct. This: 'should apply in all relevant corporate functions and operations, including procurement and purchasing decisions' (Recital 28). 'When identifying adverse impacts, companies should also identify and assess the impact of a business relationship's business model and strategies, including trading, procurement, and pricing practices' (Recital 30). This concept is not, however, reflected in the operative text of the Directive.

We believe that references to purchasing and pricing strategies designed to help deliver the objectives of the Directive should be included throughout the due diligence process described in it. Since the precise circumstances vary between sectors, potential measures that companies could adopt, applying to both buyers and suppliers, could helpfully be set out in more detail in sector-specific guidelines (see Section 9).

## 4 Material scope: human rights and environmental criteria

The Annex to the Directive lists the sources of human, social and labour rights which provide the criteria to which companies must apply due diligence. With reference in particular to land use and forests, and the production of agricultural commodities such as cocoa, we believe that this should be strengthened by the addition of references to the following three elements.

First, the list of the rights of land tenure and access, which are critical to sustainable land governance and management, must be completed to include all relevant conventions and documents. This should include, consistently with the principles in the Voluntary Guidelines on the Responsible Governance of Tenure, the UN Declaration on the Rights of Indigenous Peoples, ILO Convention 169 on Indigenous and Tribal Peoples, and other relevant documents, respect for local communities' and indigenous peoples' community and land tenure rights in all forms, whether they are public, private, communal, collective, indigenous, women's or customary rights, and the procedural right to give or withhold their free, prior and informed consent.

Second, it must include the right to an adequate standard of living, including a living income, as a fundamental human right, as embedded in Articles 23 and 25 of the Universal Declaration of Human Rights and Articles 7 and 11 of the International Covenant on Economic, Social and Cultural Rights. For smallholder farming households, living income is an important element to reach an adequate standard of living, and is defined as: 'the net annual income required for a household in a particular place to afford a decent standard of living for all members of that household' (as defined by the Living Income Community of Practice). The inclusion of a clear reference to living income would contribute to smallholder farming households sharing in the benefits of the transition to sustainable agricultural production; poverty lies at the root of many of the problems of human rights abuses and environmental degradation which the Directive is intended to address. Sectoral guidance should include references to methodologies on calculating living income levels and its key elements.

Actions taken by companies can have a significant impact on the likelihood of farming households earning a living income, and as such should fall within the same criteria as the due diligence obligations. These actions include, among others, the provision of farmer support, interventions to improve farming profitability, improving access to inputs, and reforming purchasing and pricing practices, including promoting long-term arrangements (see Section 3). At the same time, we recognise that some circumstances are beyond companies' control. The actions and policies of other actors, in particular governments, have a considerable impact on farmer incomes; the provision of affordable baseline health care, education and social services, for example, are essential in ensuring an adequate standard of living. Enforcement of a company's implementation of its due diligence obligations should take into account the extent of the company's involvement and leverage over its suppliers, as described in Section 2.

## 5 Company size

As we have argued in our previous paper: 'As recognised in the UN Guiding Principles, the responsibility to respect human rights applies to all companies regardless of their size, sector, operational context, ownership or structure ... the human rights and environmental due diligence legislation should apply to all companies registered or operating in the EU regardless of their legal form or size, including state-owned enterprises. We recognise that smaller companies may possess simpler supply chains. We do not believe, however, that these companies should be exempted from

the due diligence obligation. In a very fragmented end market, the inclusion of smaller players is critical to establish a level playing field and to ensure that all companies do their part and work closer together to improve the sustainability of the cocoa sector.’

Accordingly, we believe that all companies larger than micro-enterprises (defined as companies which employ fewer than 10 persons and whose annual turnover and/or annual balance sheet total does not exceed €2 million) in all sectors should be covered by the requirements of the Directive. (This is consistent with the position we have adopted with regard to the Deforestation Regulation.) We recognise that SMEs are likely to need additional support in introducing due diligence frameworks, but there are already several relevant provisions in the existing text. In addition, we suggest an extended implementation period for SMEs from the entry into force of the Directive.

## **6 Engagement with stakeholders**

The due diligence process described in the proposed Directive includes a number of references to engagement with stakeholders, but these are limited to consultations with potentially affected groups in gathering information on actual or potential adverse impacts (Article 6(4)), and in developing prevention action plans and corrective action plans (Articles 7(2)(a) and 8(3)(b)); and these consultations are only to take place ‘where relevant’, in the opinion of the company.

We believe that the Directive should more clearly recognise the need for meaningful and continuous engagement with affected stakeholders or their legitimate representatives: an ongoing process of interaction and dialogue between a company and its actually or potentially affected stakeholders that enables the company to hear, understand and respond to their interests and concerns, including through collaborative or joint approaches between a company and its suppliers to ensure a coordinated and coherent dialogue. A stronger requirement for meaningful and continuous engagement should be written into the Directive as part of each stage of the due diligence process. Special efforts should be made to engage with particularly vulnerable groups, including smallholders and indigenous peoples and local communities, and engagement strategies should be gender-sensitive.

## **7 Due diligence process**

In practice, judging whether a company’s efforts to implement its due diligence obligations are commensurate with the risks of adverse human rights and environmental impacts present in its operations and supply chains is likely to be a difficult task for member state enforcement authorities. There is a strong case, therefore, for taking steps to ensure that the due diligence processes companies put in place are designed to be as comprehensive and robust as possible.

The design of a company’s due diligence process – the policies and measures it puts in place to fulfil the due diligence obligations set out in the Directive, particularly in Articles 5 to 11 –should therefore be one of the elements taken into account by member state supervisory authorities in assessing companies’ compliance with their obligations under the Directive. Guidance and examples of best practice should be developed and promoted, possibly as part of sector-specific guidelines, or possibly by the European Network of Supervisory Authorities to be established under the Directive, or both.

## 8 Access to justice

As we argued in our 2021 due diligence paper, the Directive should require member states to fulfil the provisions of the UN Guiding Principles whereby states must take appropriate steps to ensure those affected by abuses have access to effective remedy through judicial, administrative, legislative and other appropriate means, including provisions for civil liability.

We welcome the fact that the Directive includes the above-mentioned requirement on member states. The extent of civil liability should take into account the extent of a company's involvement:

- If a company has caused or may cause an adverse impact, it should cease, prevent or mitigate the impact and remediate any harm if the impact has occurred.
- If a company has contributed or may contribute to an adverse impact, it should cease, prevent or mitigate its own contribution to the impact, and use or increase its leverage with other parties to prevent or mitigate it. It should also contribute to remediating the harm if the impact has occurred, to the extent of its contribution.
- If a company has not caused or contributed to an adverse impact, but its operations, products or services may be linked to an impact through a business relationship (as we argue in Section 2, we prefer this term to 'established business relationship'), it should use or increase its leverage with other parties, including suppliers, to seek to prevent or mitigate the impact.

In practice, the complaints processes of those companies directly sourcing from suppliers in producer countries are likely to be those most accessible and therefore most heavily used. However, companies further down the supply chain should establish their own complaints processes

## 9 Sectoral guidelines

We welcome the provision, in Article 13, for the Commission to issue sector- or impact-specific guidelines to accompany the Directive. We believe these will be essential to the effective implementation of the due diligence requirements, since the mix of risks of adverse human rights and environmental impacts, the socio-political framework surrounding them, and the potential steps available to companies, for example over disengagement (see Section 2) or purchasing strategies (see Section 3), varies significantly between sectors – as illustrated by various aspects of the cocoa sector we have referred to at several points above. Other issues specific to the cocoa sector include, for instance, the need to take measures jointly with producer-country governments to tackle child labour, to contribute to living income levels, or to establish farmer registration or national traceability systems. These will be especially important in the context of indirect supply chains, common in the cocoa sector, partly because of government requirements on cocoa purchasers.

We therefore call on the Commission to start the process of drawing up sector-specific guidelines as soon as possible. These should build, where appropriate, on existing approaches adopted by many companies in the cocoa sector for responsible business conduct and the avoidance of adverse human rights and environmental impacts, including child labour and deforestation.

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