MVO Platform position paper on due diligence and certification

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The most important international norms for Responsible Business Conduct – the OECD Guidelines and the UN Guiding Principles (UNGPs) – require companies to perform due diligence in order to proactively identify, prevent and reduce risks in their supply chain, and to be accountable for these actions. Sustainability certification occupies an increasingly important place in the debate on Responsible Business Conduct (RBC). What is the relationship between the use of certification systems and due diligence as mandated by international RBC norms? Due diligence is a continuous process, in which certification can play a part, but can never replace due diligence.

This document further elaborates this standpoint of the MVO Platform. It details how the concepts of certification and due diligence relate to each other, but does not discuss the implementation and impact of certification and due diligence.

What is due diligence?

In the OECD Guidelines and UNGPs, due diligence is the guiding principle for supply chain responsibility. Due diligence is the effort that companies are required to make to mitigate the negative impacts of their chains. The main characteristics of due diligence are:

- Due diligence is a **continuous** process to achieve sustainable supply chains, in which companies continuously and proactively identify, prevent and/or mitigate their actual and potential negative impacts on society, and report on this process.
- Due diligence concerns the responsibility of a company for its **entire supply chain**: in its own operations as well as in the purchase of raw materials or products and the outsourcing of business activities.
- Due diligence does not focus on the risks for, and rights of, the company, but on the **risks of business activities for society** as a whole and, in particular, for those **who are directly impacted**.

What is sustainability certification?

Certification systems differ greatly from each other, which makes it difficult to generalise about them. A product or company is certified when it meets a set of criteria (the standards) that apply to that particular certification system. This is monitored by means of regular audits. Audit reports indicate the degree to which a company complies with the defined standard as well as which actions it must take within a specified time period to address wrongdoings or other reported deviations from the standard. Many certification systems can be recognised by means of a logo or label on products.

Depending on the criteria set and the quality of the system, sustainability certification can be a key instrument for companies to identify the sustainability risks in their (often complex) supply chains, promote sustainable development, reduce the risks of human rights violations, and create stakeholder involvement. Some certification systems (such as Fairtrade, see Box below) offer additional programmes, besides the certification itself.

Private vs. public

A fundamental characteristic of a certification system is that it concerns a private, voluntary initiative, developed by companies, the sector, or multi-stakeholder initiatives. Companies can usually choose for themselves whether to make use of a specific standard or certification. Western companies do sometimes request or require their suppliers to obtain a specific certification. Voluntary certification systems stand in contrast with government policies such as legislation, in which the government sets the requirements, determines which companies must comply with them, and conducts independent monitoring. Due diligence is part of the RBC norms (which are currently still voluntary in most countries) that governments impose on companies.

Major differences between certification systems

There are major differences in quality between certification systems, which makes it difficult to draw general conclusions about them. These differences in quality are determined by:

- who the owner is of the scheme (the company itself or a multi-stakeholder initiative);
- the scope of the standard (which links in the chain are covered)
- the exact criteria of the standard (which rights are covered)
- the frequency, quality and independence of the audit;
- the standard's level of transparency.

These differences determine in part to what degree a specific system can be a useful and reliable instrument in the due diligence process of companies. The most important elements of due diligence are described below, with an explanation of how each relates to certification. This list is not exhaustive.

Risks

Due diligence concerns all risks of negative impact in the supply chain of a company. In carrying out due diligence, a risk analysis by the company itself is necessary, after which the company sets its priorities. Because the process is ongoing, new risks, if they arise, can be identified and addressed promptly. In this way, companies continuously work on improvements.

- ➔ Certification systems do not always cover all risks and often do not focus on detecting new, unknown risks and immediately including them in their approach. Community rights on which a company has impacts, for example, have only been integrated into a small number of standards.
- ➔ Certification systems can possibly play a role in identifying new risks. Expertise on supply chains and direct contact with stakeholders, as well as the insights gained from audit reports, can be used for this.

Supply chains

Due diligence concerns the responsibility of companies throughout the entire supply chain: the primary producers, surrounding communities and all links in the chain, including the company itself. It also concerns all business operations: thus, all the chains (of all products or raw materials) which a company deals with.

- ➔ Certification systems often do not extend beyond the first supplier, or focus exclusively on the primary producer. In addition, certification systems usually only apply to certain products or ingredients, instead of all the supply chains a company uses.

Collaboration

Due diligence calls on companies to collaborate where necessary to address risks and to prevent human rights abuses. This could mean that companies and suppliers make agreements in order to help one another to address risks within the chain. Collaboration within the sector, with governments or with other stakeholders, might also be necessary. Collective action can influence or increase the leverage of companies and complex problems can be addressed more effectively.

- ➔ Audit data often primarily belongs to the cooperative or the plantation itself, and detailed data often cannot be shared with certification systems without permission due to privacy restrictions. This is part of the reason that companies only examine their own operations, and thus lose the opportunity to jointly tackle risks. Certification systems often do not address supply chain relationships publicly.
- ➔ In the meantime, some certification systems have gone further, based on the view that addressing complex problems, such as living wage, demands additional measures to supplement certification. A joint approach with other stakeholders could be part of this, such as in programmes that address child labour or deforestation.

Continuity

Due diligence is a continuous process that requires an ongoing commitment from companies to take pro-active, concrete and immediate action in order to prevent negative impacts.

- ➔ Most certification systems work with tools such as audits and checklists, which report on a specific moment in time. This makes them reactive: a potential negative impact can often only be identified after it has occurred at individual suppliers.
- ➔ Here, too, there are large differences between certification systems. A certification system based on a developmental model regularly adjusts its standard as needed, based on stakeholder engagement, and requires companies to have a management system with more continuity and a proactive approach.

Transparency

An important part of due diligence is that companies communicate about their policies and how they work to eliminate and prevent risks in their supply chains. Transparency towards external actors is crucial, in particular with those that potentially could be affected by these risks.

- ➔ Certification systems do not provide public information on companies' efforts nor on the achievements of their specific suppliers. Audit reports can often only be requested by buying companies. This is less transparent than what is necessary for due diligence – which is problematic, especially when adverse impacts have been identified.

Remedy

Companies have the responsibility to offer victims remedy or compensation when they have caused or contributed to violations. The UNGPs call on companies to establish complaint mechanisms. These mechanisms could signal problems in an early stage and offer victims access to remedy.

- ➔ Most certification systems do not include provisions for remedy. When a violation of the rules has been identified, certified companies are required to take action to adapt their policies and operations. Non-compliance could result in revocation of the certificate, in the most extreme case, but this would usually not lead to remedy for the victims. However, some certification systems do have a complaint mechanism.

> **Fairtrade**
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> Fairtrade is an example of a system that in many aspects goes further than other standards, and has developed a range of additional programmes besides its standard. For instance, Fairtrade sets requirements not only for the producer but also for the producers' buyers. Non-negotiable price conditions and a complaint mechanism with follow-up and remedy are also included in the certification system. Farmers own a 50 per cent share of the Fairtrade system. Fairtrade works with a developmental model that, in addition to audits, makes use of improvement plans, programmes in which other companies and actors participate, and other supporting activities, such as investments in the capacity of small farmers.

Further reading:

- More information on differences between standards can be found in the online database of the International Trade Centre or in the Finnwatch report 'Perspectives on the quality of social responsibility monitoring schemes' (2016).
- Many multi-stakeholder standards are members of ISEAL, an international alliance that aims to further strengthen sustainability standards.