



**Ceres**

# Investor Primer on Non-Compliance Protocols: Ending Deforestation at the Source

**ENGAGE** *the* **CHAIN**

[engagethechain.org](http://engagethechain.org)

April 2019





## Introduction

Supplier non-compliance protocols are an essential part of a risk management plan for companies with exposure to commodities. Yet a lack of consensus on how to engage non-compliant suppliers has stalled many companies' implementation of no-deforestation commitments. An absence of clear protocols to deal with non-compliance will continue to allow product produced on deforested land to enter global supply chains.

Advances in satellite monitoring and activist campaigns have continued to highlight agricultural deforestation happening in tropical biomes, tying environmental destruction to name brand companies. Numerous companies have commitments to end deforestation in their supply chains, but it is often unclear how they act to end non-compliance from their suppliers. Public pressure on companies to act quickly in instances of non-compliance will only increase over time, and failures to respond will result in continued reputational risks to companies and potential negative financial impacts on investors. This investor issue brief aims to provide investors with useful information in preparation for their direct company engagements, and to facilitate stronger commitments that will end commodity-driven deforestation.

As a core component of ensuring sustainability standards, companies need to implement a monitoring and verification process to confirm that suppliers are compliant with no-deforestation policies, and then manage any non-compliance in their supply chains. It is vital that companies are able to demonstrate to investors and consumers that they can hold suppliers accountable for any failure to enforce policies. In order to efficiently resolve these issues and prevent reputational or financial loss, a company needs to implement a comprehensive plan on non-compliance — one that is publicly understood and that either brings suppliers back into compliance or removes them from the company's supply chain.

The following guide outlines key components of a supplier non-compliance protocol. Herein you will find questions to ask companies in dialogues concerning their non-compliance protocols; explanations of each component; and current best practices in non-compliance protocols.

# Components of a Supplier Non-compliance Protocol

## 1. Does the company have a protocol for supplier non-compliance?

In order to properly manage risk, companies need to publish a public document outlining their protocols for managing supplier non-compliance. Non-compliance protocols are essential to demonstrate commitment to company sustainability policies and show stakeholders companies are effectively managing the various legal and reputational risks that can stem from these incidents. These protocols need to include clear definitions and guidelines for defining non-compliance.

As a basic component of risk management, companies establish policies and procedures to handle a myriad of supplier issues. Today, many companies already have in place a no-deforestation policy, or multiple, commodity-specific policies that apply to their suppliers. However, given the complexities of these high-risk

supply chains and the likelihood that products produced on deforested-land will enter the global supply chain, it is vital that companies have a clear procedure in place to ensure that policies are being upheld as stipulated in contract relationships.

Supplier assurance is essential to the effective implementation of no-deforestation policies. Deforestation policies — if not properly enforced through active supplier assurance and clear non-compliance protocols — expose companies to reputational damage and the loss of market access. Therefore, companies must have a clear approach to supplier engagement, monitoring and verification and mechanisms for handling grievances and supplier non-compliance.

### COMPANY EXAMPLE

#### BUNGE'S PALM OIL NON-COMPLIANCE POLICY

**Policy Excerpt:** *Bunge recognizes the risk of non-compliance by prospective suppliers, whether direct or indirect. Bunge will conduct appropriate due diligence to assess whether prospective suppliers have complied with our policy from February 2017, and if necessary identify appropriate conservation / compensation / restoration measures to be carried out, prior to entering into any contracts. Bunge takes responsibility for ensuring that our Sustainable Palm Oil Policy is communicated to all our suppliers.<sup>1</sup>*

**Explanation:** *Bunge's non-compliance policy for palm suppliers is relatively strong. The identification and tracking of any breaches (for both direct and indirect supplier mills) will be subject to oversight by Bunge's grievance committee and any non-compliant suppliers may be subject to suspension and need to engage in a time-bound action plan to be back in compliance.*

**Potential Area of Improvement:** *Bunge does not specify criteria for suspension or define the upper limits of an acceptable time-bound action plan. Bunge disclosed in October 2018 that it had suspended nine farms (out of 98 that had deforested) for inadequate engagement, but did not provide a clear rationale for the suspensions nor for continued business with the other farms — leaving investors unsure on how to assess the company's commitment to engaging with suppliers in an expedited manner.<sup>2</sup>*

A supplier non-compliance document needs to be understood by suppliers and shared publicly on the buying company's website. The document should include a number of provisions, including a statement of general guidelines for engaging non-compliant suppliers and defining non-compliance by explicitly referencing the buying company's no-deforestation

policy. This policy should make clear that the buying company will develop a plan with the non-compliant supplier to bring them back into compliance, explain the instances in which the company will continue or discontinue sourcing from the non-compliant supplier, and identify any particularly egregious breaches that may result in immediate termination of a contract.

### COMPANY EXAMPLE

#### WILMAR'S SUPPLIER GROUP NO DEFORESTATION, NO PEAT, NO EXPLOITATION POLICY

**Policy Excerpt:** *Effective from January 2019, suppliers involved in deforestation and/or new development on peatland will face immediate suspension of sourcing. However, to avoid suspensions from inadvertently contributing to a growing "leakage market" or negatively impacting oil palm smallholders, post-suspension engagement is crucial, enabling us to assist suppliers in bringing their operations to compliance.<sup>3</sup> Additionally, Wilmar committed to "intervene if a supplier, or a company linked by ownership, is involved in activities that are non-compliant with NDPE policy, even when we do not procure palm oil from the particular mill or plantation, or do not intend to do so in the future."<sup>4</sup>*

**Explanation:** *In December 2018, Wilmar updated its supplier non-compliance policy in partnership with AidEnvironment to a now industry-leading standard.<sup>5</sup> This policy clearly states that Wilmar will suspend egregious forms of non-compliance with its palm oil policies and that the company will engage with suppliers to bring them back into compliance. Wilmar also publicly discloses instances of non-compliance and regularly updates stakeholders on the progress of engagement with non-compliant suppliers, as discussed further in Section III of this brief.*

## 2. Does this protocol specify criteria for potential suspension or termination of contracts and facilitate agreements to time-bound action plans for suppliers to return to compliance?

The business risks associated with continuing business as usual with non-compliant suppliers require that companies have protocols in place to assure a sustainable supply of product. When non-compliance is discovered and purchasing is suspended, companies should also work to establish a time-bound action plan with their supplier to bring them back into compliance.

Not all instances of non-compliance will require termination of contracts. Companies buying at-risk product should establish clear guidelines for when temporary suspension or possible permanent exclusion of suppliers is appropriate to ensure swift action is taken when non-compliance is found. This kind of decision making helps companies manage the potential business risks associated with continuing business relationships

with non-compliant suppliers and mitigates any negative financial impact. Decision criteria need to be well documented in the supplier non-compliance protocol and properly shared with all applicable suppliers.

Campaign pressure to ensure companies maintain extended supply chains that are 100 percent deforestation-free also puts pressure on companies to act quickly to engage, suspend or even terminate suppliers. Recently, Mighty Earth announced a “[Rapid Response](#)” system to monitor deforestation linked to agricultural supply chains. A satellite data monitoring system allows Mighty Earth and its partners to identify and document emerging and ongoing cases of companies involved in deforestation and peat development. This system will keep companies under diligent oversight and will facilitate public pressure on companies to act quickly in instances of non-compliance.

In 2018, Wilmar suspended sourcing from a supplier named in a Greenpeace report for causing deforestation in Indonesia.<sup>6</sup> Additionally, as noted in the [Ceres Case Studies on Business Risks](#) report, IOI Group experienced negative financial impacts when it was suspended from the Roundtable on Sustainable Palm Oil (RSPO) in 2016 after reports of deforestation. Purchasers including Unilever, Kellogg, Nestlé and 24 others suspended contracts with IOI Group after the RSPO suspended the company for illegal land clearance in Indonesia. These suspensions negatively impacted IOI Group revenue, resulting in the threat of a downgrade by ratings agencies. These instances and others illustrate the potential for serious financial repercussions when companies lack a proper non-compliance policy and the ability to quickly demonstrate adequate due diligence.

## COMPANY EXAMPLE

### CARGILL'S SUSPENSION OF SUPPLIERS POLICY

**Policy excerpt:** “Where forests intersect with our agricultural supply chains, we will evaluate, and will suspend, business with suppliers who are confirmed, through a credible source, audit or verification, to be in violation of our forest policy, and unwilling to remediate non-compliance issues or concerns.”<sup>7</sup>

**Explanation:** Cargill established this policy with feedback from Proforest and TFT to ensure non-compliant suppliers could be brought back into compliance and remain in business with Cargill. The company conducted a number of in-country workshops with civil society partners to develop corrective action plans and recommendations for suppliers. These efforts will assist Cargill in ending deforestation in their supply chain by informing future engagements with suppliers that are non-compliant.<sup>8</sup> Cargill also states that suppliers are expected to “strive to reduce environmental impact through efforts such as ending deforestation, minimizing greenhouse gas emissions and waste, and using resources efficiently.”<sup>9</sup>

**Potential Area of Improvement:** Cargill does not define specific criteria for when contracts will be temporarily suspended versus permanently excluded nor provide any timeframe for suppliers to be brought back into compliance. These additional disclosures could greatly improve Cargill's non-compliance protocols by clarifying how Cargill standardizes responses to non-compliance.



For more details on how to establish policies to identify and address non-compliance in supply chains, companies can refer to the [Accountability Framework Core Principles 2 and 3](#) and the [Operational Guidance on Supply Chain Management](#).

Just as when companies establish time-bound no-deforestation commitments, any plan to bring a supplier back into compliance should include a deadline for meeting the sourcing company's standards. A deadline ensures that the buyer of the product can see tangible results and demonstrates that the supplier has the appropriate systems in place to remain in compliance

with the buyer's policies. Additionally, the supplying company should continually be able to demonstrate progress toward compliance through a monitoring, verification and reporting mechanism to the buying company. Ensuring a deforestation-free supply of product requires constant monitoring of the supply chain, and active supplier assurance mechanisms will prevent future business losses for both buyers and suppliers. Setting a time-bound action plan will help incentivize the supplier to meet no-deforestation sourcing standards and ensure a sustainable supply for the buying company.

## COMPANY EXAMPLE

### NESTLÉ'S TIME-BOUND ENGAGEMENT PLAN

**Policy excerpt:** Nestlé "considers three years as sufficient time for suppliers to show material progress towards delivering traceability and meeting our Responsible Sourcing Guidelines, and five years as the maximum time that it should take to be able to demonstrate compliance. We will support suppliers who are willing to proceed towards meeting the RSGs, and exclude suppliers who are unwilling to comply with them. We will conduct regular field audits of existing suppliers to determine their performance against the RSGs."<sup>10</sup>

**Explanation:** Nestlé is one of the only companies that discloses any limit to completing time-bound action plans for suppliers when they are found non-compliant. Currently, Nestlé considers three years sufficient time for suppliers to show material progress towards delivering traceability and meeting their Responsible Sourcing Guidelines, and five years as the maximum time that it should take to be able to demonstrate compliance. Nestlé also offers direct support to suppliers who are willing to engage in this process while moving to exclude those that are unwilling to comply. Nestlé also undertakes regular field audits of existing suppliers to monitor compliance — a proactive, leading industry approach.

**Potential Area of Improvement:** It is unclear if Nestlé suspends purchasing from non-compliant suppliers or continues sourcing while engaging. Engagements with Nestlé should include discussion about the five-year time limit and opportunities to shorten this timeframe.

It is also important that buyers are transparent about why suppliers are excluded from their supply chain. Transparency provides future and current suppliers with further incentive, and reference information, to maintain compliance with sourcing protocols. It also

demonstrates to investors and other stakeholders that the buying company took a measured approach when considering termination of contracts and permanent exclusion of suppliers.

### 3. Does the company disclose information on suppliers who are not in compliance with its deforestation policy?

In order to transparently manage the various financial risks associated with non-compliant suppliers, companies should disclose the names of suppliers who are non-compliant and on the path to compliance. Previously, civil society advocates and other stakeholders have called for companies to simply and quickly end business relationships with suppliers found to have deforested land — but such actions do not get to the root of the problem and allow such suppliers to continue to supply from deforested lands to other buyers.

Ceres' recent review of supplier assurance protocols across 15 of the largest companies in the soy supply chain highlighted a need to improve protocols across the board: only two of these companies have strong supplier assurance mechanisms and they currently cover direct suppliers only. Therefore, buying companies need to practice transparency by publicly disclosing suppliers that are not in compliance with their no-deforestation policies, as well as when they are required to be back in compliance to remain a supplier.

#### COMPANY EXAMPLE

##### WILMAR'S GRIEVANCE PROCEDURE AND DISCLOSURE

**Policy excerpt:** "This Grievance Procedure has been established for Wilmar to address grievances from parties, including individuals, government organizations and non-governmental organizations concerning the implementation of Wilmar's No Deforestation, No Peat, No Exploitation (NDPE) Policy. The Grievance Procedure also promotes transparency and accountability, through disclosure of our full list of grievances, with updates on our actions to address them."<sup>11</sup>

**Explanation:** Wilmar publishes various grievances filed against the company, including a short report categorized by subject matter, the date the complaint was received and progress updates, with citations. This system allows Wilmar to address grievances and complaints while illustrating its non-compliance enforcement and remediation process. Additionally, this practice allows stakeholders to understand how Wilmar makes suspension and termination decisions with suppliers, adding transparency to their sourcing decisions that gives confidence to Wilmar's customers and investors.



## Additional Follow Up Questions for Investor Engagements

In addition to the three main framing questions used in this brief, investors can also utilize the following questions in engagements with companies to understand their current risk management strategies in reference to supplier assurance and non-compliance. These questions can be posed to any company with considerable supply chain exposure, but have been developed for use particularly with food and beverage companies sourcing commodities such as palm oil, sugar, cattle, coffee, cocoa and more.

### 1. Does the company have a protocol for identifying and addressing supplier non-compliance?

- a. Is the protocol publicly disclosed?
- b. Is it shared with all prospective and current suppliers?
- c. How does the company actively monitor compliance?

### 2. Does this protocol specify criteria for the temporary suspension or potential exclusion of contracts and facilitate agreements to time-bound action plans for suppliers to return to compliance?

- a. Does the company disclose criteria for suspension or termination of suppliers?
- b. Does the company have criteria for suspension or termination of suppliers that are not publicly disclosed? Why?
- c. Does the company require that non-compliant suppliers commit to a time-bound action plan to remedy issues?
- d. Does the company disclose the upper limits of an acceptable time-bound action plan for suppliers to return to compliance? If not, why?

### 3. Does the company disclose the names of suppliers who are not in compliance with its deforestation policy?

- a. If the company does not disclose this list, is it regularly maintained for private purposes?
- b. How does the company actively manage this list (through active use of tools such as WRI Forest Watch, Mighty Earth's Rapid Response System, or other tools)?
- c. Does the company utilize a grievance system to investigate potential supplier non-compliance? If not, why? If yes, how are stakeholders (workers, NGOs, etc.) engaged in this system?

## ENDNOTES

- 1 Bunge. (2018). *Sustainable Palm Oil Sourcing Policy*. [https://www.bunge.com/sites/default/files/bunge\\_sustainable\\_palm\\_oil\\_sourcing\\_policy.v3.1.18.pdf](https://www.bunge.com/sites/default/files/bunge_sustainable_palm_oil_sourcing_policy.v3.1.18.pdf)
- 2 Chain Reaction Research. (2018). *The Chain: Bunge's Updated Sustainability Policy Does Not Address Legal Deforestation*. <https://chainreactionresearch.com/the-chain-bunges-updated-sustainability-policy-does-not-address-legal-deforestation/>
- 3 Wilmar. (2018). *Join Statement: Creating a deforestation-free palm oil supply chain, stepping up efforts in supplier group mapping and engagement*. <https://www.wilmar-international.com/sustainability/wp-content/uploads/2018/12/JOINT-STATEMENT-FINAL-07122018-with-Signatures-v3.pdf>
- 4 Wilmar. (2019). Proactive Supplier Monitoring: Supplier Group NDPE compliance. [https://www.wilmar-international.com/docs/default-source/default-document-library/sustainability/supplier-group-compliance.pdf?sfvrsn=714f6297\\_0](https://www.wilmar-international.com/docs/default-source/default-document-library/sustainability/supplier-group-compliance.pdf?sfvrsn=714f6297_0)
- 5 Wilmar. (2018). *Join Statement: Creating a deforestation-free palm oil supply chain, stepping up efforts in supplier group mapping and engagement*. <https://www.wilmar-international.com/sustainability/wp-content/uploads/2018/12/JOINT-STATEMENT-FINAL-07122018-with-Signatures-v3.pdf>
- 6 Reuters. (2018). *Wilmar halts buying from suppliers accused of deforestation by Greenpeace*. <https://www.reuters.com/article/us-wilmar-greenpeace/wilmar-halts-buying-from-suppliers-accused-of-deforestation-by-greenpeace-idUSKBN1JL160>
- 7 Cargill. (2015). *Cargill Policy on Forests*. <https://www.cargill.com/doc/1432081368071/forest-policy-sept-2015.pdf>
- 8 CDP. (2017). Cargill Forests Survey submission, 2017. <https://www.cdp.net/en/responses/2802>, F10.1.
- 9 Cargill. *Cargill Supplier Code of Conduct*. <https://www.cargill.com/about/supplier-code-of-conduct>
- 10 Nestlé. (2011). *Commitment on Deforestation and Forest Stewardship*. [https://www.nestle.com/asset-library/documents/media/statements/2011-nestle\\_commitments\\_on\\_deforestation\\_forest\\_stewardship.pdf](https://www.nestle.com/asset-library/documents/media/statements/2011-nestle_commitments_on_deforestation_forest_stewardship.pdf)
- 11 Wilmar. (2019). Grievance Procedure. <https://www.wilmar-international.com/sustainability/grievance-procedure>

## ABOUT CERES | [WWW.CERES.ORG](http://WWW.CERES.ORG)

Ceres is a sustainability nonprofit organization working with the most influential investors and companies to build leadership and drive solutions throughout the economy. Through powerful networks and advocacy, Ceres tackles the world's biggest sustainability challenges, including climate change, water scarcity and pollution, and human rights abuses

Support for this series was provided by the Gordon and Betty Moore Foundation as part of a conservation and financial markets collaboration among Ceres, World Wildlife Fund (WWF) and World Business Council for Sustainable Development (WBCSD).

## REPORT AUTHOR

Christie Merino, Senior Associate, Food & Forests

We would also like to thank our colleagues at Ceres who provided extensive support with the project, including Dr. Julie Nash, Siobhan Collins, Mary Ann Ormond, Alba Muñoz, Larissa Witte and George Grattan.

Our thanks to Dr. Leah Samberg of Rainforest Alliance/Accountability Framework Initiative, who generously shared her time and expertise to review and provide feedback on this report.

## DISCLAIMER

Ceres reports are offered to our Investor Network. Ceres is not an investment adviser and makes no recommendations regarding advisability of investing in any particular company, investment fund or other vehicle. The information used to compile this report has been collected from a number of sources believed to be accurate that are available in the public domain.

## CONTACT FOR MORE INFORMATION

Christie Merino, [merino@ceres.org](mailto:merino@ceres.org)  
Senior Associate, Food & Forests