

Towards sustainable cocoa supply chains: Regulatory options for the EU

Executive Summary

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This paper is designed to inform the debate around potential European Union regulation of cocoa and cocoa products entering the EU market. It describes a range of options for possible action and discusses their advantages and disadvantages.

Background

Cocoa is an important source of income and employment for rural populations, particularly for the five to six million small-scale farmers who grow over 90 per cent of the world's cocoa. Nevertheless, most cocoa growers live in poverty, and the cocoa poverty trap has led to the widespread use of child labour. In addition, cocoa is a major driver of deforestation, particularly in Côte d'Ivoire and Ghana, which between them account for about two-thirds of global production and two-thirds of EU imports. In both countries, poor standards of governance and weak law enforcement also underlie many of the problems; at least 30–40 per cent of cocoa produced in Côte d'Ivoire is thought to be illegal.

There have been many voluntary initiatives to tackle these problems, such as certification schemes and company programmes.

There is increasing acknowledgement, however, that while these current initiatives have had some positive impacts, they have not succeeded, and are not likely to succeed, in tackling low prices and poverty, child labour, deforestation and illegality across the whole cocoa sector.

Certification schemes and company programmes do not cover the majority of cocoa farmers and have no direct control over some issues essential to farmers' livelihoods. Not all companies active in the EU markets have adopted commitments or programmes to tackle the problems. And while companies may be able to improve standards where they buy cocoa beans directly from farms, this is much more difficult in the widespread indirect supply chains featuring traders and middlemen. National traceability systems are also inadequate or lacking.

More broadly, issues which have major impacts on conditions in the cocoa sector – such as land and forest governance and law enforcement; land-use and cocoa sector planning; the determination of national cocoa prices and annual cocoa production levels; and education policy – are all government responsibilities. This makes them difficult for external stakeholders to influence and means they cannot be addressed by certification or company schemes applying at the farm or supply chain level alone. Perhaps most importantly, systemic weaknesses in governance and law enforcement, including the prevalence of corruption, undermine many efforts to achieve sustainable production at the national level.

The case for and objectives of EU action

The European Commission is already considering options for EU-wide action to reduce the impact of EU consumption on forests globally, potentially adapting the approach taken in the EU Forest Law Enforcement, Governance and Trade (FLEGT) Action Plan agreed in 2003. There is also growing interest in measures to limit the negative impacts of business activities on human rights, labour standards and the environment, along the lines set out in the United Nations (UN) Guiding Principles on Business and Human Rights. This has led, so far, to legislation of various types in France, the Netherlands and the UK, as well as some jurisdictions outside the EU.

Since the EU is the world's largest importer of cocoa and cocoa products, EU consumption, and any standards it imposes on imports, has the potential to affect the conditions of production in the countries of origin. There is, accordingly, a strong case that EU-wide government action or regulation should be considered, but as yet there is no consensus on what it might be. This paper discusses eight possible options for EU action, in most cases drawing on the experience of similar measures applied to other commodities or products. Most of these options are not mutually exclusive, and various combinations are possible. These options are also applicable to other commodities associated with negative environmental and human rights impacts such as deforestation or forced or child labour.

One of the issues that needs to be agreed is the standards that EU regulation is aiming to achieve. Four broad sets of aims cover the main negative impacts of cocoa production:

1. Respect for the laws of the producer country, including laws relating to: human rights; forced and child labour; employment conditions, such as minimum wages and health and safety conditions; rights of ownership and access to land; and environmental protection, including the protection of forests.
2. Respect for international human rights and labour law, including prohibitions against forced and child labour; the protection of decent working conditions; the right to a living wage for workers and a living income for smallholders; and the right to free association.
3. Improvements in governance and law enforcement.
4. The promotion of higher standards in cocoa production than provided in national laws, including: improved protection for rights of tenure, ownership and access to land; higher labour and living standards, such as improved incomes facilitated by guaranteed minimum prices and other interventions; and higher environmental standards, particularly relating to the protection of forests, such as a prohibition on deforestation, the maintenance of existing shade trees or requirements to plant new trees.

The options are grouped under three broad headings:

1. Producer-country-focused options

These options focus on actions to influence conditions in cocoa-producing countries.

Option A envisages the EU negotiating bilateral agreements with the main cocoa-producing countries, and providing financial and capacity-building assistance, to achieve the agreed standards for cocoa production in the producer country and improve standards of governance and law enforcement. This is complementary to almost all of the options discussed below and could form a valuable component of a broad package of measures addressing cocoa production and consumption. This option is modelled on the Voluntary Partnership Agreements (VPAs) between the EU and timber-exporting countries under the FLEGT Action Plan. VPAs are designed to ensure that all timber products exported to the EU have been legally produced – once products are FLEGT-licensed, they gain easier access to the EU market. Although it has proved difficult and time-consuming to establish the licensing systems, the process of negotiating and implementing VPAs has in some cases significantly improved governance and law enforcement, making the forest sector more transparent and accountable, and reducing illegal logging. This model could be adopted to cocoa, either based on the legality of production or on wider objectives.

Photo: Francisco Sierra



Option B is a 'carding' system through which the EU enters into dialogues with countries that export cocoa to the EU and issues yellow cards (warning) or red cards (notification of high risk) to those countries not combatting illegal behaviour in the supply chain. This is based on the EU Illegal, Unreported and Unregulated (IUU) Fishing Regulation, which has proved effective in encouraging several countries to improve standards. There may be scope to examine whether the early warning element could be used in conjunction with bilateral agreements similar to VPAs. This could be further combined with a due diligence regulation discussed below, to serve indicate of risk level of the producer country.

2. EU-market-focused options

These options involve measures applied to the EU market, or to a specific segment of it, products bought by government purchasers.

Under **Option C**, governments would use their public procurement policies to require that cocoa or cocoa products purchased by government buyers meet minimum criteria for legality and high social and environmental standards. All EU Member States are significant purchasers of food and catering services, and most already possess frameworks for sustainable procurement; many have adopted timber procurement policies to restrict buyers to legal and sustainable timber products. In practice, applying this approach to cocoa would probably mean that public purchasers would need to rely on cocoa certification schemes and company programmes; while this would be a step in the right direction, it is unlikely to achieve major change in the cocoa sector.

Option D sees this approach extended to the entire EU market, through a requirement that all cocoa and cocoa products placed on sale on the market meet minimum criteria for responsible sourcing – or, possibly, be produced legally. As with public procurement policies, this should have an impact, mainly through increasing the uptake of cocoa certification schemes and company programmes for responsible or sustainable sourcing. It may, however, trigger a challenge under World Trade Organisation (WTO) trade disciplines, and is a less flexible and probably slower approach than the due diligence regulations included in Options F and G.

3. Business-focused options

Under **Option E**, EU competition law is clarified or amended to allow businesses greater freedom to collaborate for sustainability purposes, factor in externality costs and, in particular, address low prices paid to farmers. In practice, competition law aiming to protect consumers against anti-competitive conduct by businesses can have a chilling effect on collaboration in pursuit of sustainability outcomes, particularly on

issues such as low prices and farmer incomes which lie at the root of many of the cocoa sector's problems. Competition law could be given a broader interpretation – either through clarifications issued by the competition authorities or by rewriting the legislation – to allow businesses to collaborate for long-term sustainability purposes.

Option F envisages a regulation requiring enterprises placing cocoa or cocoa products on the EU market to scrutinise their supply chains for the risk of handling illegally produced cocoa, or cocoa not produced to high social and environmental standards, and to publish regular reports on the extent of the risk. There is no requirement to act other than to publish the report, but it is assumed that this in itself would create an incentive for action because of increased transparency. This builds on several reporting initiatives, including CDP's voluntary system for reporting on forest risk commodities, the UK Modern Slavery Act and the EU Non-Financial Reporting Directive. However, most of the large cocoa and chocolate companies already report significant amounts of information, and this has not succeeded in resolving the problems.

Option G proposes a regulation in which all enterprises placing cocoa or cocoa products on the EU market must have in place a system of due diligence to minimise the risk of their handling illegally produced cocoa, or cocoa not produced to high social and environmental standards. In practice this would mean they would need to have information about the original source, an analysis of the risk

of non-compliance with the agreed aims, and a strategy to mitigate the risk of non-compliance. This is modelled on the EU Timber Regulation, which has helped to exclude illegal timber from the EU market, and the Conflict Minerals Regulation. Both require companies to have due diligence systems in place. Cocoa could be included in a wider due diligence regulation covering all forest risk commodities, with its application phased by commodity. It could play a valuable role in providing an incentive to cocoa-producing countries to agree a bilateral VPA-type agreement.

Option H proposes a broader regulation under which companies operating in the EU would be required to have in place a system of due diligence aimed at minimising the risk of breaches of human rights, fundamental freedoms and health and safety rights and of environmental damage in their operations and supply chains. Companies would be required to implement a due diligence plan to avoid such impacts, and to publish reports on progress. This is modelled on the French *Devoir de Vigilance* law of 2017, and similar proposals being put forward in other countries. It is not specific to any commodity or product, but covers operations and supply chains in general, though specific guidance could be issued for individual supply chains, like cocoa. This has advantages over the commodity-focused due diligence approach of Option G, in that it avoids the need to legislate commodity by commodity, or sector by sector, but it does represent a major change in business practices, and in practice could be slower to implement and is more likely to be restricted only to the largest companies.

Conclusions and recommendations

As the major global consumer of cocoa from Ghana and Côte d'Ivoire, the EU has a critical role to play in improving the problems of the cocoa sector. There is, however, no simple or single solution. Rather, action is required at many levels and by many actors. None of these options in isolation is likely to succeed in encouraging the development of a sustainable cocoa supply chain which meets the aims of ensuring respect for human rights and labour standards, payment of fair prices, protection of the environment and improvements in governance and law enforcement.

A package of options to be implemented by the EU and its Member States, however, could have much greater impact. **Option A (bilateral agreements) would help trigger essential action by producer-country governments. Either Options G or H (due diligence regulation) would directly affect the behaviour of companies in the cocoa supply chain that operate in the EU, and could help to provide an incentive to producer-country governments to sign such an agreement. Option E (review of competition law) should help companies address the problem of low prices for producers and may also be necessary to enable the inclusion of criteria relating to prices and remuneration in a due diligence regulation.**

None of the options described in this paper are easy to implement; all will face challenges and barriers. But the need for action is clear. It is to be hoped that discussion on the options outlined here may contribute to efforts to find a solution.

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