Independent Retail Europe

POSITION PAPER
ON SUSTAINABLE CORPORATE GOVERNANCE
- COMMENTS OF INDEPENDENT RETAIL EUROPE -

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COMMENTS OF INDEPENDENT RETAIL EUROPE ON SUSTAINABLE CORPORATE GOVERNANCE

We welcome the opportunity to comment on the EU initiative on sustainable governance. Sustainability is a key topic for all economic sectors, driven by consumer demand and a strife to distinguish one's business from one's competitors. The EU already has extensive legislation for environmental and social protection with which companies have to comply and for which they are liable. Furthermore, consumers and social media are playing an important role as a driver for sustainability by calling companies out on non-sustainable behaviour and obliging them to pay more attention to their impact on and their role in society. **EU companies**, **therefore already integrate sustainability risks, impacts and opportunities into their long term strategies.**

A. Considerations specific to groups of independent retailers

1) Independent Retail Europe represents retail groups characterised by the provision of a support network to independent SME retail entrepreneurs; joint purchasing of goods and services to attain efficiencies and economies of scale, as well as respect for the independent character of the individual retailer. Our members, as cooperative/associative structures have unique corporate governance structures whereby the independent member retailers have the oversight of management – including Directors – and strategy of the group. These groups were established with the objective of safeguarding the long term competitiveness and sustainability of its independent retailers. Retailers, as consumer facing operators are in a constant listening mode with the public and society as a whole. They already have strong stakeholder involvement mechanisms and structures in place as their success depends how they are perceived by consumers. They are constantly in contact with, and therefore also under the scrutiny of, the public. Placing this responsibility with Directors will not make this more effective. Independent retailers are local entrepreneurs. Profits are invested back into local communities through local spending but also via the sponsorship of local events, teams and community projects. This "local touch" extends to stocking local products as well as promoting local and regional development. This is through building close relationships with local or regional producers, as well as service providers, ensuring that the local/regional economy benefits. Therefore, **by their nature, groups of independent retailers give preference to the interests of their local community and the long term sustainability of the group over the financial interests of the (member) shareholders. Indeed, the long term sustainability of the group is a prerequisite for the sustainability of its members and therefore always balanced against the short term interest of the shareholders.**

A legislative initiative should not negatively affect groups of independent retailers' existing processes for involving stakeholders and balancing interests.

2) **For groups of independent retailers, a general obligation of due diligence for the whole of the supply chain which would apply equally to the wholesale organisation of the groups as well as to the individual retailers in the group would lead to unnecessary duplication and therefore to an unnecessary burden. The central wholesale organisation and its member retailers should not be required to carry out due diligence to the same extent with regard to the same products just because they are separate legal entities. This would also be discriminatory as in an integrated chain it would only be the chain itself who would apply due diligence, not the individual stores, as these are part of the same entity.**

Any due diligence requirements of retailers belonging to a group needs to be light touch and limited to the products of and the relations with their direct external supply chain partners.

B. Considerations with regard to due diligence, Directors' care and stakeholder involvement

As part of their strategy, groups of independent retailers, mostly through third party certification, **already voluntarily adhere to many initiatives and standards that have environmental or social sustainability for their objective**. For example: Fairtrade, the Rainforest Alliance and Forest stewardship (FSC) and the SA8000 SAI social accountability standard, the Partnership for Sustainable Textiles, the Forums for Sustainable Cacao and Palmoil, the Responsible Business Alliance (RBA), the Amfori Business, Social and Environmental Compliance Schemes for trade with third countries, the ISCC of the Consumer Goods Forum, Global GAP/Grasp as well as many individual retailer-specific initiatives e.g. the sustainable sourcing of bananas and oranges, the reduction of plastic packaging, better animal welfare standards or short supply chains. Furthermore, in the food sector a European Code of Conduct for responsible business and marketing is currently in the process of being drafted. EU-wide recognition of these standards and initiatives is essential. An EU initiative should therefore not seek to reinvent the wheel by setting out processes for due diligence, as this would lead to unnecessary costs for supply chain actors who already make substantial investments and efforts to make their supply chains more sustainable; it should rather set **a general framework for due diligence** with a clear focus on human rights and practicable criteria for implementation (with further qualifications, see below).

As a start, a mapping and recognition of these standards and initiatives would be useful.

In addition, an **EU legislative initiative should ensure that all supply chain actors apply due diligence with regard to human rights in a manner commensurate to their size, role and the risk of infringement.** This way, companies can meet their obligations with reasonable effort and continue to build on good experiences and best practices.

The initiative should be accompanied by political measures. In developing and emerging countries, over 60% of people work in the informal sector. Here, the **primary responsibility for compliance with human rights rests with the states and their governments**. The international community must therefore not let up in its efforts to demand and enforce human rights in the local working environment. We believe that strengthening international and multilateral cooperation, especially in the course of more intensive development cooperation, is central.

1) The scope of an EU initiative for sustainable governance / due diligence

Transparent supply chains include digitization, secure documentation and efficiency as well as an additional **right to information from upstream operators on data from the supply chain**, **which does not exist today**. A general requirement of due diligence, and as defined by the EU: *"**processes** to **prevent, mitigate and account for** human rights, health and environmental impacts, including climate change, **both in a company's own operations and its supply chain**"* is simply not feasible for retailers. **The size and complexity of retailers' assortments and supply chains, particularly in the food sector, makes it impossible for retailers to guarantee such far reaching due diligence processes and would require a disproportionate effort and cost**.

Retailers are part of a **global, highly complex value creation and economic system**. They are subject to intense international competition. **Supply relationships are by no means linear chains, but rather highly differentiated value-added networks with constantly changing sources of supply and highly flexible logistics processes**. This is especially true in the food industry with its diverse value-added networks for globally produced raw materials. This complexity increases immensely in the case of composite foods with a large number of raw materials from different origins. In addition, key raw materials are often grown exclusively in high-risk countries (e.g. cocoa), which usually have insufficient legal enforcement. For decades, European companies have been trying to bring about lasting improvements through social standards, industry initiatives and NGO partnerships. It must also be taken into account that there is a lack of transparency on the part of suppliers with a strong market position (global brand industry, large raw material bundles). The protection of competitive advantages and data make traceability in supplier networks even more difficult. Both the **complexity, the risk exposure of the countries of origin and the flexible logistics processes mean that control and liability up to the origin is impossible for retailers.**

According to the European Commission, due diligence "*should be inherently risk-based, proportionate and context specific, implying that the extent of implementing actions should depend on the risks of adverse impacts the company is possibly causing, contributing to or could foresee*". **We fully agree with this approach, but this needs to be more clearly defined to give companies legal certainty that their due diligence efforts towards sustainability are sufficient**.

We therefore **favour a tiered responsibility, focusing on human rights, commensurate to the size and type of the company and to the risk per commodity/product group/area with a safe harbour approach.**

a) **Due diligence with a tiered responsibility**

First of all, the scope of due diligence, in line with EU rules on a retailers' responsibilities in the supply chain, should be **limited to the activities under their direct control and in connection with their direct contractual partners (tier 1), who should be obliged to provide the necessary information**. Otherwise, there is a risk for damages that the company cannot control and of a lock-in effect of suppliers as well as a disengagement of risky markets, which may be detrimental for local economies. Due to the size and complexity of their product ranges, retail companies cannot monitor the value chain at all times from the end of the chain to the producer level. For instance, when a supplier delivers a product promising / guaranteeing that the product is safe, or the production sustainable or the packaging recyclable, etc. **The retailer should be able to rely on this information as it is not feasible for him to check everything.** Suppliers should be obliged to provide this information and the retailer should also be able to ask for such information, where this is needed and missing.

The concept of tiered responsibility also entails that a retailer, as a distributor, **can only take responsibility for his own brands**. Due to the complexity and changeability of supply chains as well as business and recipe secrets, a retailer is not in a position to oversee, let alone influence, supply chains and production conditions for products from brand manufacturers.

b) **Due diligence that takes account of the group business model**

As explained above, particularly for groups of independent retailers, a general obligation of due diligence would lead to unnecessary duplication and therefore an unnecessary burden: If a retailer's due diligence were not limited to the activities under his direct control and in relation with his direct

supply chain partners, this would lead to a duplication of efforts and costs for groups of independent retailers, as each wholesale organisation and each retailer in the group would be required to apply due diligence to the whole of the chain, resulting in an unnecessary doubling of administrative efforts and costs. Thus, **any due diligence requirement needs to avoid unnecessary burdens for groups of independent retailers.**

c) **Thematic due diligence, focusing *only* on human rights**

A due diligence requirement for environmental sustainability would constitute an unnecessary burden with no added value for EU retailers as there is already a plethora of EU and national initiatives, both legislative and non-legislative, which envisage environmental sustainability with which EU retailers need to comply, and more are in the pipeline. The existing legislative and voluntary framework is a fully adequate, legally certain framework for compliance. We therefore see no added value in a due diligence initiative for environmental sustainability since retailers are already liable when they fail to comply with the regulatory requirements.

Likewise, EU retailers already have to comply with extensive –mostly- national, and comparable legal frameworks for social responsibility. This should continue to fall under the remit of the Member States and the EU, as foreseen in the Social Pillar. **A due diligence requirement for the retail sector with regard to social responsibility would therefore also constitute an unnecessary burden without added value for EU retailers.**

We therefore believe that the initiative should solely focus on the human rights standards recognised in the UN Guiding Principles. These consist according to UN guideline 12.2 of the principles in accordance with ILO-Core conventions (no forced labour, children labour or discrimination and freedom of coalition), of the General Declaration of Human Rights and international agreements about civil and political rights as well as about economic, social and cultural rights.

d) **Due diligence commensurate to the risk**

In any case, **any initiative and the burdens it entails, should also be proportionate to the risk of the area and the commodity of infringement of human rights**.

We believe that he European Commission already has thorough knowledge on the global state of play of governance structures, applicable laws, enforcement mechanisms and their effectiveness in the different countries and regions, as well as the risks certain products may entail. Inspired by the EU legal system established in the context of illegal fisheries[1], the Commission should use this existing knowledge and network and establish **commodity and country related risk analysis lists.** The Commission should divide product categories/commodities (sportswear, textiles, leather goods, electronics, food etc.) up in high, medium and low risk commodities, relative to the extent in which these commodities as well as the areas where they are purchased, are likely to affect human rights, with suitable rules for each of the three risk categories:

- Areas without risk
- Areas with moderate risk
- High risk areas

1 European IUU Fisheries Regulation No. 1005/2008

As in the fisheries system, these lists should be regularly monitored and updated. The Commission will give guidance what elements and political developments contribute to reducing the identified risk factors. Stakeholders will have the opportunity to report observed human rights infringements towards the local representative of the European Commission.

Based on the risk categorization, undertaken by the European Commission (via regular analysis of the legal acquis, existing enforcement mechanisms, effectiveness of enforcement and directly and indirectly detected and reported human rights violations), companies have to fulfil mandatory due diligence requirements in the following manner:

- No risk region > no due diligence requirements
- Moderate risk region > medium due diligence requirements
- High risk (red listed countries) > heightened due diligence requirements (not a complete prohibition of imports)

Incentives created by such a system:

- Additional due diligence requirements for areas with a lack of protection and enforcement of human rights will create market incentives for goods originating from countries taking positive action this will help goods manufactured/sourced with a high level of protection of human rights to become the easiest choice;
- Countries are interested in fostering positive developments and enforcement of rules in order to achieve a low risk rating // Countries should no longer experience incentives towards lowering national standards
- Companies have to intensify their due diligence activities based on the risk connected to their sourcing markets // Companies receive independent assessments of the situation on the ground and can undertake their risk management in the context of legal certainty and knowledge that they have information at hand that can be trusted
- NGOs, trade unions and other relevant stakeholders on the ground have the option of feeding into the assessment via a safe, confidential and protected dialogue with the European Commission delegations

Suggestions for Implementation

- Following a risk-based approach, the EU institutions should set out a roadmap for step by step evaluation and integration of commodities under the new system

e) **Due diligence commensurate to the size of company**

SMEs play an important role in many EU supply chains, particularly in the food supply chain. Fully exempting SMEs from due diligence would present an additional risk for downstream operators in the chain. This could make these operators refrain from dealing with SMEs. We therefore **suggest to nevertheless apply a regulatory approach for those SMEs that other stakeholders in the chain rely on to undertake due diligence whereby, as a minimum, SMEs should have an obligation to provide the necessary information on their process, sourcing, product, packaging etc. to ensure that other companies in the supply chain are able to undertake due diligence assessments.** In this regard, SMEs should be subject to lighter requirements and receive capacity building support. In addition, detailed

non-binding guidelines catering for the needs of SMEs as well as dedicated national helpdesks are necessary for companies to translate due diligence criteria into business practice.

The due diligence of retailers, as these are at the end of the chain, should in any case be limited to the business under their control and to direct contract partners.

f) **Geographical scope of a due diligence initiative**

The initiative should apply to all third country business operators doing business in the EU, also those with headquarters outside of the EU. This requires close cooperation with third countries, and adaptation of trade agreements, so as to avoid distortions of competition. In this context it would be conceivable to introduce a due diligence system in accordance with the model of the European IUU Fisheries Regulation No 1005/2008, which relies on incentives for positive behaviour of countries/states. In line with risk categorisation carried out by the European Commission (through regular analysis of the legal acquis, existing enforcement mechanisms, effectiveness of enforcement and directly and indirectly identified and reported human rights violations), the mandatory due diligence obligations of companies could be differentiated according to the identified level of risk.

Liability:

Due diligence towards human rights should cover the adverse effects on human rights that a company causes through **its own activities or that are directly related to its business, products or services or relationships**. An exclusive focus on tier 1 and only on the direct contractual partners is necessary. Liability beyond tier 1 would lead to an overstretched and disproportionate understanding of liability. Accordingly, **companies must not be prosecuted for violations that are beyond their direct control. The same applies to violations that a company is unable to detect despite compliance with the duty of care (duty of effort instead of duty of success)**. Furthermore, there should be no criminal or civil liability.

Safe Harbour Approach:

We request the EU take a Safe Harbour Approach. **According to such an approach, the fulfilment of independent standards and participation in multilateral partnerships in the context of the structuring of due diligence obligations must be taken into account**. An internationally recognized and standardized Safe Harbour acceptance point and an associated process should be established that defines clear criteria. The criteria for using such an approach to recognition of standards should be clear, unbureaucratic and externally verifiable.

Reporting and documentation obligations:

Reporting and documentation obligations are currently already being implemented in many cases by companies by publishing sustainability reports. New reporting obligations in the course of this due diligence initiative should therefore be avoided. Instead, the EU should advocate a **common, international standard for sustainability reporting**. Instead of creating a new EU reporting standard from scratch, existing standards should be analysed and built upon. When publishing future reports, it needs to be ensured that **sensitive company and business information is protected** from potential misuse. A transfer of company-sensitive data

to third parties must be excluded as well as publication on the internet. Likewise, competition law restrictions regarding the exchange of company data must be taken into account.

Reporting obligations should be proportionate (reporting to authorities, no general publication). In addition, the EU should advocate a common, international standard for sustainability reporting.

Transition period:

With regard to the implementation deadline, companies will need a reasonable amount of time. A transition period of at least 5 years to set up such systems should be considered.

2) Obligations of Directors – duty of care and due diligence

Directors already have an obligation by law to act in the benefit of the company (duty of care). What constitutes the benefit of the company often lacks clarity and is open to interpretation. **A better, harmonized definition of the role of Directors** would avoid that this is interpreted to mean short term interests of the shareholders, and short term financial interests of Directors.

Directors' obligations under the initiative should be limited to efforts towards due diligence processes and an obligation to report on these efforts. They should be accountable with regard to the processes and reporting thereon, but cannot be directly accountable for any harm. We are in favour of giving Directors responsibilities in this regard within the scope described above: **in relation to the respect of human rights** and limited to the **business under their control** and **in relation with direct contractual partners** (tier 1) who should be obliged to provide the necessary information.

Directors should not be liable for harm when adequate due diligence processes and reporting were in place, or for activities beyond their control. Equally, Directors should not be liable for a lack of due diligence where the infringement and harm could not be avoided, i.e. Directors should have a duty of effort towards due diligence and reporting on this duty of effort, not a duty of result.

Companies – not individual persons - should have a general obligation to have sustainability goals and with regard to this a legal obligation to balance short and long term interests. This could contribute to a level playing field. **Which, and to what extent, interests are taken into account should remain at the discretion of the companies, not of individual persons, and be limited to strategic decisions and to decisions concerning payments of dividend.** In case of the latter, it would be a good solution if the EU were to impose an obligation on Directors of quoted companies to always balance the shareholders' interests against the long term interest of the company, the interests of employees, clients and society.

In any case, the issue of preferring short term shareholder benefit over long-term stakeholder interests only applies to quoted companies and is therefore only relevant in this context, and not in relation to not quoted companies.

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independent member retailers have the oversight of management –including Directors- and strategy of the group. These groups were established with the objective of safeguarding the long term competitiveness and sustainability of its independent retailers. Retailers, as consumer facing operators are in a constant listening mode with the public and society as a whole. They already have strong stakeholder involvement mechanisms and structures in place as their success depends how they are perceived by consumers. They are constantly in contact with, and therefore also under the scrutiny of, the public. Placing this responsibility with Directors will not make this more effective. Independent retailers are local entrepreneurs. Profits are invested back into local communities through local spending but also via the sponsorship of local events, teams and community projects. This "local touch" extends to stocking local products as well as promoting local and regional development. This is through building close relationships with local or regional producers, as well as service providers, ensuring that the local/regional economy benefits. Therefore, **by their nature, groups of independent retailers give preference to the interests of their local community and the long term sustainability of the group over the financial interests of the (member) shareholders. Indeed, the long term sustainability of the group is a prerequisite for the sustainability of its members and therefore always balanced against the short term interest of the shareholders.**

A legislative initiative should not negatively affect groups of independent retailers' existing processes for involving stakeholders and balancing interests.

No interference in Directors remuneration

The initiative should not interfere with Directors' remuneration. A better legal definition of the role of Directors would have sufficient an impact. (See above)

3) Stakeholder involvement

Stakeholders already play a role in companies' decisions, as companies identify and voluntarily exchange with relevant stakeholders on strategic decisions that are likely to have an impact.

With employees this happens in a more regulated context via the representative organisations of employees. **Beyond the latter, it should be left to the companies to engage with stakeholders where they deem this necessary. A consumer facing sector such as retail, is by nature of its business in a constant listening mode to consumers and society.**

Companies should not have an obligation to balance all stakeholders' interest nor for each decision. First of all, companies may not be aware of all different stakeholders in respect of each decision, and secondly, this would put companies' competitiveness at risk as it would make the internal decision-making process too slow. Thus, **stakeholders should not be given an official role in the enforcement of the duty of care as this could lead to unnecessary delays of decisions and to unnecessary costs, and could affect the competitiveness of the company.**

4) A fully harmonized system, with harmonized regulatory enforcement

Irrespective of the scope, format and applicability the initiative should be fully harmonised and applied in the same manner throughout the EU. Enforcement needs to be regulatory as authorities should supervise it in

the same manner and according to the same standards so as not to enable companies to move to countries with less strict rules. **Any reporting requirements, regulations and measures have to be proportionate, clear and measurable.** In this regard, a thematic approach would allow for being specific in terms of requirements, standards, results, etc.

Internal enforcement within the company should be left to the company. The functioning of company councils and the role of the unions are already clearly defined in this context. **Sanctioning powers need to be clearly defined as well.**

SUMMARY

1. The scope of an EU initiative for sustainable governance

- We favour a **tiered responsibility, solely focusing on human rights, commensurate to the size and type of the company and to the risk per commodity/product group/area with a safe harbour approach;**
- **Whereby it should be remembered that the primary responsibility for compliance with human rights rests with the states and their governments;**
- **A general obligation of due diligence is impossible for retailers and would, *for groups of independent retailers, lead to unnecessary duplication and therefore an unnecessary burdens*;**
- **Due diligence should be limited to the activities under a company's direct control and in connection with their direct contractual partners (tier 1), who should be obliged to provide the necessary information; Retailers can only take responsibility for their own brands;**
- **Liability for failure to apply due diligence should be proportionate (obligation of effort, not of result; no criminal or civil liability);**
- **Existing industry-specific standards need to be recognized and a Safe Harbour Approach established, with clear, unbureaucratic and externally verifiable criteria;**
- **Reporting obligations should be proportionate (reporting to authorities, no general publication). In addition, the EU should advocate a common, international standard for sustainability reporting;**
- **A transition period of at least 5 years to set up such systems should be considered;**
- ***A legislative initiative should not negatively affect the existing processes for balancing long and short term interests of groups of independent retailers;***
- ***Any due diligence requirements of retailers belonging to a group needs to be light touch and limited to the products of and the relations with their direct external supply chain partners.***

2. The Role of Directors – duty of care and due diligence

- **There should be a better, harmonized definition of the role of Directors with a duty of care to balance short and long term interests;**
- **Directors should have a duty of effort towards due diligence and reporting on this duty of effort, not a duty of result;**

- **Directors should not be liable for harm when adequate due diligence processes and reporting were in place, or for activities beyond their control. Equally, Directors should not be liable for a lack of due diligence where the infringement and harm could not be avoided.**
- **Companies should have a general obligation to have sustainability goals and with regard to this a legal obligation to balance short and long term interests.**

3. Stakeholder Involvement

- **Stakeholders should not be given an official role in the enforcement of the duty of care as this could lead to unnecessary delays of decisions and could lead to unnecessary costs and affect the competitiveness of the company;**
- **Which, and to what extent, stakeholder interests are taken into account should remain at the discretion of the companies, not to individual persons, and be limited to strategic decisions and to decisions concerning payments of dividend.**

4. Enforcement

- **A fully harmonized system, with harmonized regulatory enforcement and clearly defined sanctions;**
- **Reporting requirements, regulations and measures have to be clear and measurable;**
- **Internal enforcement within the company should be left to the company.**

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Established in 1963, ***Independent Retail Europe*** *(formerly UGAL – the Union of groups of independent retailers of Europe) is the European association that acts as an umbrella organisation for the main groups of independent retailers in the food and non-food sectors.*

Independent Retail Europe represents cooperative retail groups characterised by the provision of a support network to independent SME retail entrepreneurs; joint purchasing of goods and services to attain efficiencies and economies of scale, as well as respect for the independent character of the individual retailer.
Our members are groups of independent retailers, associations representing them as well as wider service organizations built to support independent retailers.

Independent Retail Europe represents 24 groups and their 386.602,00 independent retailers, who manage more than 753.000 sales outlets, with a combined retail turnover of more than 944 billion euros and generating a combined wholesale turnover of 297 billion euros. This represents a total employment of more than 6.603.000 persons.

More information about Independent Retail Europe under www.independentretaileurope.eu