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FAO-OECD Guidance for Responsible Investment In Agricultural Supply Chains *(Comment Period Closes Feb. 20, 2015)*

Considerations for Sovereign and Private Investors, Food-Agri Companies, and Finance Providers

This update briefly discusses aspects of the FAO-OECD Guidance for Responsible Investment in Agricultural Supply Chains (the “Guidance”), which is open for public comment through February 20, 2015. Among other things, the Guidance proposes a risk-based due diligence approach for adoption by enterprises engaged in the agricultural supply chain. Elements of the risk-based due diligence approach are outlined (with some comment) below, followed by considerations for sovereign and private investors, food-agri companies, and finance providers (e.g., commercial banks).

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The Guidance

In January 2015, the Food and Agriculture Organization of the United Nations (FAO) and the Organisation for Economic Cooperation and Development (OECD) published, and invited public comment on, the draft “FAO-OECD Guidance for Responsible Agricultural Supply Chains” (the “Guidance”).

The Guidance is the product of a consultation process led by the multi-stakeholder Advisory Group that was established in October 2013 and includes, among others: OECD and non-OECD countries, institutional investors, food-agri companies, civil society organizations, and farmers groups.¹

Public Comment Period, Comments to be Published

Governments, businesses, civil society, international organizations,

and the general public are invited to comment on the Guidance. The public comment period closes February 20, 2015.

A compilation of comments will be published online “at the end of the consultation period.”²

Applicability to Agricultural Supply Chains

The Guidance applies to agricultural supply chains (“ASC”), i.e.: “the system encompassing all the activities, organizations, actors, technology, information, resources and services involved in producing agricultural products for consumer markets.”³

Promotes Responsible Business Conduct

Recognizing that growing demand for agricultural products (food and non-food) and services is likely to increase

agricultural investment, the Guidance is intended “to help enterprises . . . to observe standards of responsible business conduct along agricultural supply chains and ensure that their operations can contribute to economic development and food security.”⁴

Countries with Weak Governance, Insecure Land Rights of Particular Concern

The Guidance is particularly concerned with ASC activities in “developing countries where investment stocks in agriculture are relatively low” and/or have “weak governance and insecure land rights.”⁵ The Guidance includes expectations that investors and other parties with “leverage” will exert their influence to facilitate more responsible business conduct in such

countries (discussed at [table](#) below on risk-based due diligence).

“Enterprises” are Intended Users of the Guidance

Among the intended users of the Guidance are “enterprises” operating across the ASC, including those that are domestic or foreign, sovereign-affiliated and private, and range in size from small to large.⁶ Other intended users include governments, civil society, and constituencies affected by ASC activities.

Sovereign and Private Investors, Food-Agri Companies, Finance Providers

The Guidance expressly identifies sovereign investors (including state-owned enterprises and sovereign wealth funds), institutional investors (*e.g.*, pension funds), family offices, and finance providers (*e.g.*, commercial banks) as enterprises engaged in the ASC—some are described as new entrants. Food-agri companies and, more notably, business services providers are also identified as intended users.

Non-Binding by Itself,⁷ but Likely Consequential

While the Guidance itself, even if issued in final form, is/will not by itself be binding (absent incorporation into applicable binding laws), it is nevertheless relevant and likely to be consequential in concrete ways, as discussed below ([considerations for investors, finance providers, food-agri companies](#)).

Related Principles and Standards of Investment, Business Conduct

The Guidance draws upon previously issued or agreed principles and guidelines for responsible business and investment conduct (general and industry specific), including the *Principles for Responsible Investment in Agriculture and Food Systems* (Committee on World Food Security), the *Principles for Responsible Agricultural Investment that Respects Rights, Livelihoods* (FAO and others), the UN Global Compact, and the OECD Guidelines for Multinational Enterprises.⁸

Guidance Structured on OECD Conflict Minerals Due Diligence (incorporated into Dodd-Frank conflict minerals disclosure rule)

The Guidance is structured on the *OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas*, a document that has been endorsed by, among others, the U.S. Department of State and the United Nations Security Council (by resolution) (the “OECD Minerals Guidance”).

Notably, in its final rule implementing Section 1502 (conflict minerals) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the U.S. Securities and Exchange Commission (SEC) recognized the OECD Minerals Guidance as the due diligence framework to be observed by issuers subject to the conflict minerals disclosure requirement of the Dodd-Frank Wall Street Reform

and Consumer Protection Act.⁹ (relevance discussed further [below](#)).

Risk-Based Due Diligence

The Guidance sets forth a five-point risk-based due diligence framework recommended for enterprises involved in ASC.¹⁰ The five points of due diligence (all but one having sub-points), are:

- (1) Strong management systems for responsible ASC.
- (2) Systems of controls and transparency along the ASC.
- (3) Identification and assessment of risk in the ASC.
- (4) Audit ASC due diligence.
- (5) Publicly report ASC due diligence policies and practices.

These five points are described further at the [table](#) below.

Model Policy for Agricultural Supply Chains

The Guidance provides a “Model Enterprise Policy for Responsible Investment in Agricultural Supply Chains” (the “Model Policy”) for adoption by enterprises active in the ASC.¹¹ Adoption of the Model Policy is a first step of risk-based due diligence, and the Model Policy can be adopted as is or tailored for enterprises’ existing policies, risk management frameworks, and other enterprise-specific considerations.¹²

The Model Policy is discussed further at the [table](#) below, within the risk-based due diligence framework.

RISK-BASED DUE DILIGENCE (RBDD) IN AGRICULTURAL SUPPLY CHAINS (ASC)

This table identifies some elements of the RBDD approach described by the Guidance, with some commentary (italicized text, sub-bullet points).

Five Points of Guidance RBDD	Select Sub-elements of Guidance Points
<p>ESTABLISH STRONG MANAGEMENT SYSTEMS FOR RESPONSIBLE ASC</p>	<ul style="list-style-type: none"> ▪ Adopt a policy for Responsible Business Conduct in ASC. This can be the Model Policy as provided in the Guidance, or a version that is tailored for the enterprise, its operations, jurisdictions of operation, and position in the ASC (e.g., on-farm or closer to “upstream” levels of the ASC or for “downstream” activities further removed from, e.g., production), etc. ▪ Policy should enable and further functions and objectives of RBDD, be informed by relevant experts (internal and external), reflect applicable legal and other obligations, and be incorporated or reflected in operational policies of the enterprise. ▪ Policy may include industry-specific standards or protocols (as applicable and relevant). ▪ Policy should be approved and credibly endorsed at senior-most level. ▪ Designate senior level responsibility for policy implementation. ▪ Implement training and incentives designed to facilitate effective execution of policy. ▪ Designate technically and culturally competent personnel to take due diligence responsibility, with backing of appropriate financial and human resources. <ul style="list-style-type: none"> ○ <i>Knowledge of social culture, legal culture (e.g., informality as to land tenure and resource rights, etc.), and political culture (and therefore political risk) is key, particularly in countries with weak governance and (typically associated) political risk propensity.</i> ▪ Establish effective internal reporting structure. ▪ Conduct and follow-up on environmental, social, and human rights impact assessments (ESHRIAs). ▪ Establish protocols to effectively trace agricultural products and create and retain records of same.
<p>IDENTIFY AND ASSESS RISKS IN SUPPLY CHAIN</p>	<p>Two levels of due diligence: ordinary and enhanced (both conducted at the outset and on an ongoing basis, as appropriate).</p> <ul style="list-style-type: none"> ▪ Identify, in advance of investment/engagement in particular ASC activity, relevant risks associated with relevant asset(s), activity type(s), parties (business partners, affected parties, government entities), etc. ▪ Apply enhanced due diligence (“heightened managerial care”), where, e.g.: “red flag locations” are involved (presence of conflict, weak governance, human rights violations, etc.); business partner practices raise red flags; or, relevant agricultural products are associated with adverse environmental, social, or human rights impacts.
<p>DESIGN AND IMPLEMENT STRATEGY TO RESPOND TO IDENTIFIED RISKS</p>	<ul style="list-style-type: none"> ▪ Disclose findings of risk assessment to senior level management. ▪ Provide risks findings to “affected stakeholders and business partners.”¹³ <ul style="list-style-type: none"> ○ <i>The extent to which findings of risk assessments (and other information) can or should be shared with “affected stakeholders and business partners” will vary by enterprise type, investment type, and other factors. There should be a balance between disclosure to achieve common goals and preservation of proprietary or other confidential of information.</i> ○ <i>There is an issue also of how counterparties or “affected stakeholders” act with respect to the use and non-disclosure of third-party information.</i>

	<ul style="list-style-type: none"> ○ <i>Parties disclosing information (even with confidentiality or limited distribution conditions) should consider whether disclosures in good faith may later create or contribute to liability or other legal, commercial, reputational, or political risk for the disclosing party.</i> ○ <i>The final version of the Guidance should consider and account for legitimate concerns of private actors (particularly those more further removed from on-farm or “upstream” activities).</i> ■ Adopt and implement comprehensive risk management plan(s) that include, among other things, contingency plans. ■ Leverage position to “help build capacities for due diligence efforts” of on-farm and upstream actors. <ul style="list-style-type: none"> ○ <i>This element of RBDD is illustrative of the Guidance’s expectation (or desire) that “downstream” actors (e.g., investors) will use their “leverage” to facilitate more transparent, compliant, and less risky conduct by other parties, through, e.g., capacity building, contractual provisions, and other measures.</i> ○ <i>This expectation merits consideration, as downstream actors may not possess the “leverage” that is assumed, particularly in environments where governance is weak, legal recourse is limited or of diminished value (e.g., in food security-driven investments where money damages or other legal remedies are inadequate), and/or opacity obstructs access to reliable information.</i> ○ <i>Also, consideration should be given to the financial and other costs to private parties of capacity building to the extent needed to produce the results the Guidance apparently seeks. Related to this is the question of whether the proponents of such capacity building or other efforts will contribute, or procure contributions to, capacity building on a broader scale.</i>
<p>COMMISSION AN AUDIT OF SUPPLY CHAIN DUE DILIGENCE</p>	<ul style="list-style-type: none"> ■ Procure independent third party audits of RBDD at strategically “identified points” in the supply chain. Audits may also focus on, but not to the exclusion of other key areas, context specific “choke points” in the ASC. ■ Ensure that audits conform to RBDD objectives and policies, as well as applicable or relevant laws and standards. ■ Permit auditors, where appropriate, to “coordinate efforts in order to recognize audit conclusions from other independent third party audits carried out for other purposes.” Relevant aims here are developing “complementary and mutually-reinforcing systems against common standards,” and promoting efficiency.¹⁴ <ul style="list-style-type: none"> ○ <i>This element of the RBDD approach illustrates the Guidance’s preference, in appropriate places, for collaboration among parties in the ASC. Here again, issues of confidentiality and overall feasibility are relevant, and require further consideration/clarification.</i>
<p>REPORT ON SUPPLY CHAIN DUE DILIGENCE</p>	<ul style="list-style-type: none"> ■ “Enterprises should publicly report on their supply chain due diligence policies and practices, with due regard taken of business confidentiality and other competitive concerns.”¹⁵ ■ Public reports may include “information on enterprise management systems, the risks assessments it has carried out, the steps taken to manage risks, and audit reports of due diligence practices. They should be accessible to all relevant stakeholders.”¹⁶ <ul style="list-style-type: none"> ○ <i>Here, the Guidance specifically considers enterprise concerns as to confidential and private information. The final version of the Guidance should go further, e.g., by speaking to the scope and feasibility of such public reporting. A more specific delineation of “relevant stakeholders” should be provided and “public reporting” should be clarified to indicate whether “public” is unlimited (e.g., for unrestricted public consumption or “public” meaning limited to defined parties).</i>

CONSIDERATIONS FOR SOVEREIGN AND PRIVATE INVESTORS, FOOD-AGRI COMPANIES, FINANCE PROVIDERS

The Guidance is Relevant

While, as noted above, the Guidance is not and will not (in draft or in final form) by itself be binding, it is nevertheless relevant today.

The Guidance reflects growing consensus around problems, and potential solutions, relevant to food and agricultural investment and commercial activities, particularly involving jurisdictions in which, *inter alia*, governance is weak, land rights are unclear, transparency is lacking, effective legal recourse is limited, and political risk is relatively high.

As noted above, some of the standards or issues addressed or contemplated by the Guidance are part of binding law in various jurisdictions (*e.g.*, human rights, labor rights).

The Guidance is Likely to Become Consequential in the Near-term

Food security and agricultural investment are of global concern. The Guidance and similar standards are likely to gain greater near-term importance and usage by various parties.

As noted above, the OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas—on which the Guidance is structured—was incorporated in the SEC's final rule implementing the conflicts minerals disclosure provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act. Should the Guidance (or

similar documents) also come to be regarded as a/the leading international framework on responsible agricultural investment or other ASC activities, it may be similarly incorporated in, or directly inform, laws and regulations.

Moreover, as more jurisdictions have adopted or are considering adopting mandatory environmental, social, and governance reporting for certain entities (*e.g.*, large companies, public companies), standards such as those embodied in the Guidance will become more relevant to companies' reporting-related practices: *e.g.*, counterparty due diligence protocols, records creation and retention practices, etc.

Tracing of Agricultural Products of Particular Relevance to Food-Agri Companies

For food-agri companies in particular, expectations in the Guidance for tracing the origins and handling of agricultural products from production to movement across the ASC are obviously relevant.

Food-agri companies (particularly consumer-facing) today have commercial and legal incentives to trace agricultural products and their handling in the ASC. The Guidelines reinforce such practices and may raise expectations that they will be adopted more widely, uniformly, and effectively.

Private, Sovereign Investors With Long-Term Investment

For institutional investors such as pension funds, elements of the Guidance are consistent with their investment, governance, and corporate responsibility standards, and should be incorporated by them to the extent that doing so adds value without undue cost.

While some state-owned/affiliated entities' legal, commercial and reputational risk considerations differ from those of private investors, their adoption of protocols and objectives embodied in the Guidance may prove strategically valuable, to stabilize specific transactions and enhance long-term competitiveness.

As more sovereign and private entities enter the agricultural investment field, those with tarnished reputations (or histories of real or perceived irresponsible business practices in the ASC) will not, in the long-term, be as competitive as their counterparts.

Commercial Banks, Credit and Other Risk Assessments

Commercial banks and other finance providers may consider incorporating aspects of the Guidance where appropriate, *e.g.*: in their risk assessment tools (*e.g.* business credit environmental, ethical, and social risk scoring) to more effectively identify risk and diminish risk of entanglement in party or transaction related controversy.

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NOTES

¹ Guidance at 9.

² Guidance at unnumbered opening page.

³ *Id. at* at 9.

⁴ Guidance at unnumbered opening page.

⁵ *Id.*

⁶ *Id. at* 8-9.

⁷ Human and labor rights standards identified in the Guidance, particularly in the Model Policy for Responsible Agricultural Supply Chains, have been adopted as law in various jurisdictions. Applicable law should, as always, be reviewed and accounted for on a jurisdiction-by-jurisdiction basis. *See, e.g.*, Guidance at 19.

⁸ *Id. at* Annex IV (Description of the Main Instruments Considered in the Guidance).

⁹ *See* SEC Requirement of report regarding disclosure of registrant's supply chain information regarding conflict minerals, 17 CFR 249b.400 (2015 Lexis); Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 1502 (2010).

¹⁰ Guidance at 13, 13-18.

¹¹ *Id. at* 19-23.

¹² *Id. at* 19.

¹³ *Id. at* 16.

¹⁴ *Id. at* 17.

¹⁵ *Id. at* 18.

¹⁶ *Id.*