Fighting Slavery in Brazil: Strengthening Local Solutions

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In August 2010, Domini Social Investments, a New York City-based mutual fund manager, announced that it had reached an agreement with Nucor (NYSE: NUE), the largest steel producer in the United States, to address the company's exposure to slavery and illegal deforestation in its Brazilian supply chain.[1] The agreement followed three years of dialogue with the company.

Objectives of the Engagement

The objective of this engagement was to convince Nucor to adopt a credible and transparent set of policies and procedures to address the likelihood that slavery or forced labor is being used in its Brazilian supply chain to produce pig-iron, a key ingredient in the manufacture of steel.

Workers who labor at the bottom of corporate supply chains producing raw materials for processing by other entities are at particular risk of the most egregious human rights violations, including slavery, forced labor and child labor. While these problems may appear to be beyond company control, they can also raise significant legal and reputational risks should they come to light.

The investors involved in this engagement sought to simultaneously reduce risks to Nucor and to the Brazilians exposed to slavery. The investors recognize that Nucor is not in a position to police its entire supply chain, however, as the world's largest buyer of Brazilian pig-iron, the investors believed that Nucor had the responsibility, and a unique opportunity, to positively influence conditions on the ground.

Introduction

In 2006, *Bloomberg Markets Magazine* published a cover story on modern slavery, focusing on the production of pig-iron in Brazil.[2] Every year, thousands of workers are taken deep into the Amazon under false pretenses where they are forced to illegally harvest timber and produce charcoal under extreme and degrading conditions. The charcoal produced at these camps is used to make pig-iron, which is ultimately sold to international buyers including Nucor, one of several companies named in the story.

Slavery is a significant problem in Brazilian agriculture as well, including cattle ranching, soybeans, sugarcane, cotton and other commodities, all of which feed into the international supply chains of many global companies. Although the Brazilian pig-iron industry is responsible for only 10 percent of the cases reported to the Comissão Pastoral da Terra (The Catholic Church's Pastoral Land Commission, or CPT, profiled on page 63 of this report) between 2003 and 2010, nearly 2,000 people have been freed from illegal charcoal camps in the past five years Companies like Nucor face significant challenges in addressing this problem. First and foremost, the identities of charcoal suppliers are generally unknown to their international buyers, as they are several tiers down the supply chain. But Nucor's general counsel set the right tone when he said, "Any amount [of pig iron] that is sold with the use of slave labor is too much."

The Risks of Slavery

Slavery is an international crime, actionable under the U.S. Alien Tort Claims Act, a statute that has been increasingly used to file high profile lawsuits against corporations for human rights abuses in other countries.[3] Corporate directors have a legal and an ethical duty to ensure their companies are taking appropriate actions to avoid complicity in such abuses.

Although companies like Nucor do not have a consumer face, and are therefore less susceptible to reputational risk, their corporate customers may be household names, and may choose suppliers that can meet their social and environmental standards.[4]

1 For the Domini announcement, see: http://www.domini.com/common/pdf/SocialImpactUpdate_2010_Q1.pdf. This was also reported on the ILO's website at http://www.ilo.org/sapfl/News/lang--en/WCMS_143438/index.htm.

2 Smith, M. and Voreacos, D., "The Secret World of Modern Slavery," Bloomberg Markets. December 2006. Available at http://www.asyousow.org/publications/Slavery.pdf

3 The Second Circuit Court of Appeals, however, recently held that the Alien Tort Claims Act does not apply to corporate defendants in Kiobel v. Royal Dutch Petroleum. Individuals that work for corporations could still potentially be sued under the Act. See http://jurist.org/paperchase/2010/09/federal-appeals-court-upholds-verdict-for-shell-in-nigeria-protest-deaths.php. Earth Rights International is currently challenging this decision. See http://www.earthrights.org/legal/eri-files-brief-human-rights-and-labor-groups-challenging-corporate-immunity-abuses.

4 In November 2010, for example, Domini presented the outcome of its engagement with Nucor at a meeting of Ford Motor Company's key suppliers.

The persistence of slavery in Brazil also presents broader risks to the Brazilian economy, which should be of concern to investors seeking to invest in that region. Slavery presents an obstacle to equitable economic growth, and also carries the risk of international boycotts of Brazilian commodities 'tainted' by slave labor. Illegal deforestation also exacerbates the global threat of climate change and threatens one of the world's most critical and unique ecosystems.

The Engagement

Prompted by the *Bloomberg Markets Magazine* story, a group of signatories to the United Nations-backed Principles for Responsible Investment (PRI) formed a coalition to address the problem. This engagement began with letter-writing to companies around the world in a range of industries from steel, to auto and appliance manufacturers. Domini took the lead with Nucor,[5] and sent a letter in April 2007 to Nucor's CEO on behalf of the group.[6]

Although Nucor did not reply to the letter, the company did respond to independent inquiries from Trillium Asset Management, one of the signatories. Nucor explained that it was monitoring the Brazilian government's "dirty list" of employers found to use slaves, and required its direct suppliers to certify that slaves were not used. The company would not respond to additional questions from the investor group.

Domini and its partners on this engagement[7] submitted three shareholder proposals to Nucor in 2008, 2009 and 2010, seeking a board review assessing the company's efforts to ensure the protection of fundamental human rights in its global operations and supply chain, and a public report to shareholders. The first proposal was withdrawn in exchange for a written agreement from Nucor that produced a formal policy prohibiting forced labor in its supply chain. The investors, however, were dissatisfied with Nucor's compliance with the remaining terms of the withdrawal agreement and chose to refile, pressing the company for a more comprehensive and transparent system.

The second shareholder proposal led to Nucor's first public response to the issue, which came in the form of the Board's 'statement in opposition' in its corporate proxy statement, providing details on its response to slavery in Brazil, and explaining why shareholders should vote against the proposal.[8] Nevertheless, the proposal was endorsed by RiskMetrics Group, the influential proxy advisory firm, and received the support of 27 percent of the shares cast, a significant vote for a first-year human rights proposal, particularly for a company with no exposure to consumers.

The shareholder proposal provided Domini with the opportunity to make a statement at Nucor's annual meeting. Domini commended Nucor for the steps it had thus far taken to address slavery, but also raised a number of questions about the adequacy of its response.

The 2010 Agreement

In 2010, Domini and Nucor entered into a written agreement in exchange for the withdrawal of the third shareholder proposal. The agreement takes advantage of two important Brazilian anti-slavery initiatives, the National Pact for the Eradication of Slave Labor and the Citizens Charcoal Institute.

Throughout the dialogue, the investors encouraged Nucor to sign and adhere to the National Pact for the Eradication of Slave Labor, a multi-stakeholder effort that since 2005 has successfully engaged companies representing approximately 20 percent of Brazil's gross domestic product in the fight against slavery. The Pact is monitored by Reporter Brasil, the Ethos Institute of Business Ethics and Social Responsibility, the Social Monitoring Institute and the International Labor Organization.[9] Among a series of key commitments, Pact signatories must agree not to pur¬chase from suppliers on the government's "dirty list," and to allow independent monitor¬ing of that commitment. A number of major corporations have signed the Pact, including Cargill Agrícola S.A., Coca-Cola Brasil, Carrefour Indústria e Comércio Ltda, and Wal Mart Brasil, but no non-Brazilian company has signed.

In 2010, Nucor informed Domini that it had entered into discussions with the Citizens Charcoal Institute (ICC), an association of Brazilian iron and steel companies formed in 2004 to combat slavery in their supply chains. As a condition of membership, each ICC member agrees to subject its entire supply chain to monitoring to ensure legal and humane working conditions.

5 The Domini Social Equity Fund, Domini's flagship mutual fund, has held Nucor stock since the Fund's inception in 1991. Domini recognizes the company's substantial use of recycled steel and electric arc furnaces and employee empowerment programs.

6 The letter was signed by Domini, Catholic Superannuation Fund, Morley Fund Management, PREVI – Caixa de Previdencia dos Funcionarios do Banco do Brasil, New Zealand Superannuation Fund, Storebrand Investments, MMA, City of New York, Office of the Comptroller, and Trillium Asset Management.

7 Investors participating in this engagement included Trillium, MMA, Catholic Healthcare West, Adrian Dominican Sisters, Christian Brothers Investment Services, Sisters of the Holy Names of Jesus and Mary, US Ontario Province, Sisters of Charity of the Incarnate Word, San Antonio, Benedictine Sisters of Atchison, and the General Board of Pension and Health Benefits of the United Methodist Church.

8 See Proposal #5, available at: http://nucor.com/investor/sec/html/?id=0001193125-09-062545&sXbrl=1&compId=107115

9 The text of the National Pact is available at: http://www.reporterbrasil.com.br/documentos/national_agreement.pdf; An overview of the Pact and its work is available at: http://www.reporterbrasil.com.br/pacto/conteudo/view/9.

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Although the coalition generally favor multi-stakeholder initiatives over industry initiatives, both Reporter Brasil and the ILO have vouched for the integrity of the ICC, explaining that the two efforts are complementary. The ICC[10] monitors suppliers from the pig-iron manufacturer down to each charcoal camp, and the National Pact traces each camp on the "dirty list" up the value chain to ensure that Pact signatories are adhering to their commitment to avoid these black-listed entities.

After discussions with Domini, Nucor agreed to require all of its top-tier Brazilian pig-iron suppliers to either join the ICC or endorse and commit to the National Pact. As an additional check, Nucor agreed that it would receive audit reports from the ICC and monitor compliance by its suppliers on the basis of these reports.

Nucor also agreed to become a financial patron of ICC, helping to finance its monitoring work, and ICC agreed to open itself to new members for the first time. Although there is a risk that new ICC members will not carry the same commitment as its founding members, this agreement may help to bring the project to scale. The next few years will be an important time to monitor the ICC to ensure it retains its high reputation and record of success.

Measuring Impact

As part of its agreement with the investors, Nucor agreed to publish annual progress reports on its implementation of these policies.[11] It published its first sustainability report in September of 2010, which contains a description of these new policies. The coalition will monitor these annual reports and provide the company with feedback where appropriate, perhaps offering specific reporting metrics as the program progresses. Public reports are a standard element of most shareholder proposal withdrawal agreements, as they provide a regular mechanism for holding companies accountable to the commitments they've made.

As noted above, the company will receive audit reports from the ICC, and will use these reports to hold their suppliers accountable to their policy. These reports will remain confidential.

The investors also intend to maintain close contact with Reporter Brasil, CPT and the ILO to evaluate the success of this agreement.

Components of Success

The following were particularly important components of this engagement:

1. The shareholder proposal was a particularly important tool. Although the investor group did not hold a significant percentage of Nucor's shares, the shareholder proposal provided an important point of leverage, providing access to the company's proxy statement and its annual meeting, and providing a means of communication with Nucor's largest institutional investors. Several institutional investors contacted Domini during the course of the engagement to receive updates. Perhaps most importantly, the availability of the shareholder proposal ensures that even small shareholders can keep critical issues in front of management and the board of directors year after year.

2. Domini maintained close contact with Reporter Brasil and CPT throughout the engagement in order to better understand the nature of the problem. Domini was also in contact with the ILO. These contacts were critically important in ensuring that the investor proposals would be meaningfully targeted to solutions on the ground.

3. The existence of two successful local NGOs provided opportunities that are often unavailable to companies seeking to address labor conditions in their supply chains. Domini is hopeful that this agreement will set a helpful precedent for other international companies and industries sourcing from Brazil.

Many international corporations source a wide variety of products from Brazil, and other supply chains face even more significant risks of slavery than the pig-iron supply chain does. Agricultural commodities are particularly problematic. Companies purchasing Brazilian agricultural products should assess their exposure to slavery and engage with Brazilian civil society through the National Pact, rather than simply sourcing elsewhere. Ethical investors and companies should look to capitalize on effective local solutions to endemic sustainability problems, when they are available, rather than seek to impose external compliance systems that may not be attuned to local conditions, and may not ultimately contribute to the long term growth and sustainability of local civil society organizations. Ultimately, the success of global companies is dependent upon the health of local communities. Investors should become more adept at measuring corporate contributions – both positive and negative – to the local communities that provide the raw materials for the global economy, and include these measures in their valuation models.

10 Costa, M., and Trindade, P., Fighting Forced Labour: The Example of Brazil. International Labour Office. Geneva: ILO, 2009 at p. 98, available at http://www.ilo.org/wcmsp5/groups/public/---ed_norm/---declaration/documents/publication/wcms_111297.pdf ("The ICC's actions have contributed to improving working conditions …Through the ICC, more than a thousand charcoal kilns have been inspected, of which 316 were discredited and are prohibited from selling charcoal to iron and steel enterprises within the Institute." The report also credits the ICC with a special project to ensure that freed workers do not return to conditions analogous to slavery (see p. 109.)) 11 Nucor "2009 Sustainability Report," available at: http://nucor.com/sustainability/2009/download/Nucor_SustainabilityReport09.pdf

11 Nucor "2009 Sustainability Report," available at: http://nucor.com/sustainability/2009/download/Nucor_SustainabilityReport09.pdf