

UNOFFICIAL ENGLISH TRANSLATION

To the Ministry of Finance

April 18, 2013

**Recommendation on the exclusion of Zuari Agro Chemicals Ltd. from the
Government Pension Fund Global's investment universe**

Unofficial English Translation

1 Summary

The Council on Ethics recommends excluding the Indian company Zuari Agro Chemicals Ltd.¹ (Zuari) from the Government Pension Fund Global due to an unacceptable risk that the company through its production of hybrid seed contributes to the worst forms of child labour.

In the autumn of 2011 and 2012 the Council on Ethics surveyed the prevalence of child labour in the production of hybrid cottonseed for the company. On average 20 per cent and up to 30 per cent of the workforce used in the seed production for the company was found to be children. The Council on Ethics has based its assessment on the understanding that the company does not itself own the farms where the seed is cultivated and does not have a direct contractual relationship with the people who work there either; rather the seed is cultivated on commission from and under the supervision of the company.

The Council on Ethics has attached importance to the systematic use of children in production for the company. This is regarded as the worst forms of child labour because of the young age of the children and the health hazards they are exposed to in this work, partly as a result of the use of pesticides. The Council on Ethics has also attached importance to the fact that the risk of child labour is well known in this industry, that the company probably has a close working relationship with the farmers who use child labour, and that the company has not taken concrete steps to reduce the extent of child labour.

2 Introduction

In 2011, the Council on Ethics decided to assess the Fund's investment in the then Zuari Industries Ltd. against the Guidelines for the observation and exclusion of companies from the Government Pension Fund Global's investment universe (the GPFGE Ethical Guidelines). The background was the question of whether there was extensive use of child labour in the seed production for the company.

The seed production takes place at the company Zuari Seeds Ltd., which is now a wholly owned subsidiary of Zuari Agro Chemicals Ltd.² At the end of 2012, the GPFGE owned shares in Zuari Agro Chemicals Ltd. valued at NOK 14.5 million, corresponding to 1.5 per cent of the company's shares.

Both Zuari Seeds Ltd. and Zuari Agro Chemicals Ltd. are referred to as "Zuari" below.

The Council on Ethics has previously undertaken extensive surveys on the use of child labour in hybrid seed production for multinational companies in India. The case in hand pertains to an Indian company that was not in the GPFGE portfolio when the previous studies were conducted.

¹ Zuari Agro Chemicals Ltd. ISIN: INE840M01016

² In 2011 Zuari Seeds Ltd. was a wholly owned subsidiary of Zuari Industries Ltd. Following a restructure in 2012 Zuari Seeds Ltd is now a wholly owned subsidiary of Zuari Agro Chemicals Ltd.

2.1 What the Council on Ethics has considered

The Council on Ethics has considered the GPF's investment in Zuari in the light of section 2, 3 (a) of the ethical guidelines for the Fund:

*“The Ministry of Finance may, on the advice of the Council of Ethics, exclude companies from the investment universe of the Fund if there is an unacceptable risk that the company contributes to or is responsible for: [...] the worst forms of child labour and other child exploitation; [...]”*³

The Council on Ethics bases its assessment of whether child labour can be categorised as “*the worst forms of child labour*” under the guidelines on the wording of the UN Convention on the Rights of the Child, which in Article 32 obliges states to protect children from work that is hazardous or likely to interfere with the child’s education or development.⁴

The Council on Ethics also bases its assessments on the wording of the ILO Convention 182, which defines the worst forms of child labour, *inter alia*, as work that is likely to harm the health or safety of children. The same convention also stipulates that exposing children to any form of slavery or practices similar to slavery, including debt bondage and serfdom, is to be regarded as the worst forms of child labour.⁵

Even if it is states, as opposed to companies, that are obligated by international human rights conventions, companies can nevertheless be said to contribute to human rights violations. The Council does not take a position on the extent to which the state is responsible for any human rights violations; it is sufficient to establish that the company in question is acting in a manner that links it to serious or systematic violations of internationally recognised human rights.⁶ This applies regardless of whether the state where the violations are taking place has ratified the conventions against which the circumstances are assessed.

The Council on Ethics considers that the following elements can form the basis for the assessment of whether there is an unacceptable risk of a company contributing to human rights violations: There must be a concrete link between the company’s operations and the violations in question, and the violations must also either be ongoing or there must be an unacceptable risk that they will occur in the future. The Council has also placed much emphasis on whether the company’s operations have led to extensive and lasting negative

³ Guidelines for the observation and exclusion of companies from the Government Pension Fund Global’s investment universe: http://www.regjeringen.no/en/sub/styret-rad-utvalg/ethics_council/ethical-guidelines.html?id=425277

⁴ UN Convention on the Rights of the Child, Article 32: “States Parties recognize the right of the child to be protected from economic exploitation and from performing any work that is likely to be hazardous or to interfere with the child’s education, or to be harmful to the child’s health or physical, mental, spiritual, moral or social development.” <http://www.ohchr.org/EN/ProfessionalInterest/Pages/CRC.aspx>

⁵ ILO Convention no. 182: “For the purposes of this Convention, the term ‘the worst forms of child labour’ comprises:

(a) all forms of slavery or practices similar to slavery, such as the sale and trafficking of children, debt bondage and serfdom and forced or compulsory labour, including forced or compulsory recruitment of children for use in armed conflict; [...]

(d) work which, by its nature or the circumstances in which it is carried out, is likely to harm the health, safety or morals of children.” <http://www.ilo.org/public/english/standards/realm/ilc/ilc87/com-chic.htm>

⁶ See section 3.2 of the Council on Ethics’ recommendation on the exclusion of Wal-Mart Stores Inc., dated 15 November 2005, and section 5.1 of the recommendation on the exclusion of Monsanto Co., dated 20 November 2006 (www.etikkradet.no).

impacts for the people affected, to what extent particularly vulnerable groups have been affected, and what the company has done to improve the conditions.

Commercial hybrid seed production in India is organised such that seed companies enter into agreements with local farmers for the cultivation of seed. The company provides upfront inputs such as the seed for planting and pesticides, and visits the farms regularly for quality control and to give advice. The seed companies do not themselves use children as workers in the sense that they employ children; rather the company's link to the use of child labour is through the use of local farmers whom the children work for.

In this case, the Council on Ethics has assessed whether the use of child labour in hybrid seed production for Zuari implies that the company contributes to the worst forms of child labour.

2.2 Sources

The Council on Ethics has used a consultant to survey the extent of child labour in the production for the company.⁷ Surveys were carried out in autumn 2011 and 2012 at a total of 30 and 80 farms, respectively, in the states Gujarat, Maharashtra, Andhra Pradesh and Karnataka. The assessment is also based on the company's letters to the Council on Ethics. In addition, information has been obtained from the company's annual report and website as well as other sources.

3 Background

3.1 Child labour in the Indian seed industry in general

Despite the increased attention given to the problem in recent years there is still widespread use of child labour in the Indian seed industry. A survey conducted in 2009–2010 estimated that some 380 000 children, of whom roughly 170 000 were under the age of 14, worked in the cultivation of hybrid cottonseed in India.⁸ A similar survey conducted in 2010 estimated that some 150 000 children, of whom 60 000 were under 14 years of age, worked on the cultivation of hybrid vegetable seed in India.⁹

The cultivation of hybrid seed is extremely labour-intensive when plants have to be pollinated manually, as is the case for hybrid cotton seed. Working conditions are generally poor with long working days, physically demanding work and continuous exposure to pesticides. In some cases, children work in slavery-like conditions in debt bondage.

The Council on Ethics first began working on this issue in 2005. Since then there have been developments in several areas that have affected both the extent of child labour and various aspects linked to production in general. The Indian government, primarily the National Commission for Protection of Children's Rights (NCPR), has implemented a number of measures to reduce the use of child labour. In 2006, UNICEF initiated a programme to reduce

⁷ Research was carried out by Dr Davuluri Venkateswarlu, Glocal Research and Consultancy Services, Hyderabad, India.

⁸ Dr. Venkateswarlu (2010) "*Seeds of Child Labour – Signs of Hope. Child and Adult Labour in Cottonseed Production in India*", ICN et al.: <http://www.indianet.nl/pdf/signsofhope.pdf>

⁹ Dr. Venkateswarlu (2010) "*Growing up in the Danger Fields: Child and Adult Labour in Cottonseed Production in India*", ICN, ILRF et al.: <http://www.indianet.nl/pdf/dangerfields.pdf>

the prevalence of child labour in this industry.¹⁰ The large, multinational companies involved in the industry have come under pressure from civil society and investors regarding child labour. Not least, NBIM¹¹ has raised this issue with several of the major companies, which have introduced extensive programmes to prevent child labour in their production.¹²

Since 2007, the area under hybrid cottonseed cultivation in India has increased by over 60 per cent, from about 24 000 to 40 000 hectares. The area under cultivation for the companies that the GPFG is invested in constitutes roughly one-third of this. Much of this expansion has been in remote areas where this kind of production has not been done in the past and where there is a plentiful supply of cheap labour and little attention is given to the issue of child labour. In the states Gujarat and Tamil Nadu, the entire expansion has been in less developed areas.

3.2 About Zuari Agro Chemicals Ltd.

Zuari Agro Chemicals Ltd. produces inputs for agricultural production, primarily artificial fertilisers and pesticides, but also hybrid cotton- and vegetable seed.¹³ The company operates in India where the seed production is carried out by its wholly owned subsidiary Zuari Seeds Ltd.

In 2011 production of hybrid cottonseed for the company took place in Gujarat, Andhra Pradesh and Maharashtra and encompassed a total of about 350 hectares.¹⁴ In 2012, this had risen to some 800 hectares. This constitutes roughly 2 per cent of the total production in India. It is estimated that around 4 000 farms were involved in cottonseed production for the company in 2012.¹⁵

The company also produces hybrid vegetable seed, mainly chilli pepper, tomato and okra, primarily in Karnataka. The Council on Ethics does not have accurate data on the scope of this production, but it is estimated to encompass approx. 250 farms.

3.3 Related cases

Several rounds of studies were carried out on commission for the Council on Ethics during the period 2006–2008 to chart the prevalence of child labour in the Indian seed industry. The studies looked into production for several different companies and in different areas. A

¹⁰ UNICEF: “It is estimated that hundreds of thousands of children, mainly girls, work in India’s cotton industry alone. The vast majority of these child workers do not attend school. In many cases, children are employed because they are paid much less than adults – about \$1 per day – and work longer hours. Moreover, they can’t easily complain. Cotton production is painstaking work that requires long hours of cleaning, seeding and hauling water to fields, then standing and individually cross-pollinating each flower by hand before finally plucking every bloom. Often, child workers suffer respiratory and other health problems caused by exposure to pesticides, extreme heat and physical stress. Some are also beaten or sexually abused by employers. Since 2006, UNICEF and the IKEA Social Initiative have partnered to tackle child labour in India by building public awareness about existing laws that forbid it. The country’s child labour law prohibits the hiring of children younger than 14, but enforcement has been difficult since few children understand their rights.”
http://www.unicef.org/education/india_55444.html

¹¹ Norges Bank Investment Management (NBIM) manages the Government Pension Fund Global.

¹² NBIM: *Children’s Rights – a concern for investors*, <http://www.nbim.no/no/media-og-publikasjoner/temaartikler/2009/investor-expectations-on-childrens-rights/>

¹³ The company’s website: <http://zuari.in/>

¹⁴ 350 hectares = 3.5 square kilometres.

¹⁵ The average size of the farms included in the study was 0.2 hectares.

common feature was that in areas where measures to reduce the use of child labour had not been implemented, children often made up around 30 per cent of the workforce, in some places even more.

In 2006 the Council submitted a recommendation to the Ministry of Finance to exclude the company Monsanto Co. from the GPFG.¹⁶ The background for this was the extensive use of child labour in the production of hybrid cottonseed for the company. In this case, the Council on Ethics attached importance to the extent of the use of child labour, the young age of the children, the health risks the children were exposed to as a result of the use of pesticides, and the fact that some of the children were sent to work far away from their homes.

Since NBIM was engaged in active ownership dialogue with Monsanto and several other companies to try to influence them to adopt better measures to prevent child labour in seed production, the Council on Ethics in 2008 recommended that the Ministry of Finance maintain its investment in Monsanto, on the grounds that active exercise of ownership would probably reduce the prevalence of child labour. An important factor in this decision was the fact that NBIM was the only major institutional investor that had initiated this type of agenda with the companies, and that the GPFG's investment in the companies was a prerequisite for NBIM to be able to continue to exert this influence.

Studies that the Council had undertaken in 2011 demonstrated a significant decrease in the incidence of child labour in those companies where concrete measures to this end had been implemented. In the areas that have achieved the best results, children typically constituted between 2 and 4 per cent of the workforce in production for these companies. While the problem has not been completely eliminated, the prevalence of child labour had gone from being consistent and systematic to more sporadic.

The extent of the GPFG's investments in small Indian companies has increased in recent years. The Indian company to which this recommendation pertains, Zuari, has not been included in NBIM's active ownership dialogue and the company has not participated in the industry initiative that NBIM helped to initiate.

4 The Council on Ethics' surveys 2011-2012

On assignment for the Council on Ethics, surveys were conducted in autumn 2011 and 2012 on the prevalence of child labour in the production of hybrid cotton- and vegetable seed for Zuari. This was part of a larger survey of the use of child labour in hybrid seed production for a number of companies in India.

The purpose of the surveys was to chart the extent of child labour and practices linked to the use of pesticides on farms producing hybrid seed for companies in the GPFG in the states Gujarat, Andhra Pradesh, Maharashtra and Karnataka.

¹⁶ The recommendation and correspondence concerning the Council on Ethics' recommendation on the exclusion of the company Monsanto Co., November 2006: <http://www.regjeringen.no/nb/sub/styrer-rad-utvalg/etikkradet/Tilradninger/tilradninger/menskerettigheter/tilradning-20-november-2006-om-utelukkel.html?id=526099>

4.1 Methodology

The surveys were conducted through unannounced visits to the farms. The age of the workers was determined through conversations with workers and observations. In this study, anyone above the age of 15 years was categorised as an adult and everyone under the age of 15 years was categorised as a child. Cases where it could not be determined whether the worker was above or less than 15 years were categorised as “unsure”.

As with previous surveys of this type, children were frequently observed leaving the field when strangers approached. Where these were observed and could be counted, they were counted and categorised as children in the study.

2011

Studies were conducted at 30 randomly selected farms that produce for Zuari, 20 in Gujarat and 10 in Maharashtra, in the period from August to December 2011. The 30 farms in the sample accounted for about 2.5 per cent of the area under hybrid cottonseed cultivation for the company in the 2011 season.

2012

The working conditions were surveyed at 80 farms in 16 villages in Gujarat, Andhra Pradesh and Karnataka. Of these, 60 produced cottonseed (30 each in Gujarat and Andhra Pradesh) and 20 produced vegetable seed. The cottonseed producers in the sample accounted for about 5 per cent of the area under hybrid cottonseed cultivation for the company in the 2012 season.

4.2 The findings of the surveys

Prevalence of child labour, 2011

The total workforce on the farms visited in the study amounted to 164 people. 43 of these may have been children under the age of 15 years: 31 people were determined with certainty to be under 15; in 12 cases the individual’s age was not determined with certainty.

15 per cent of the children were under the age of 10 years old, and 90 per cent of the children were under the age of 14.

The proportion of children who were working (only including certain observations) accounted for between 15 and 20 per cent of the workforce at each farm. Including the uncertain observations, the proportion of children in the workforce was almost 30 per cent.

Prevalence of child labour, 2012

The total workforce on the farms visited in the study amounted to 1017 people, 227 of whom may have been children under the age of 15 years: 164 people were determined with certainty to be under 15; in 63 cases the individual’s age was not determined with certainty. Almost 20 per cent of the children were under the age of 10 years.

Children constituted some 10–20 per cent of the workforce at each farm (only including certain observations). Including the uncertain observations, the proportion of children in the workforce was 15–25 per cent.

The use of child labour varied according to what was being produced: the proportion of children in the production of tomato seed was around 15 per cent, whereas the proportion of

children involved in the production of cotton seed and chilli pepper seed was approx. 25 per cent.

Other findings from the Council on Ethics' research

The studies conducted in 2011 indicate that roughly half of the children working on the farms were contract workers; the others had family ties to the farms. There were equal numbers of boys and girls. The studies conducted in 2012 found that almost 80 per cent of the children were contract workers. Two-thirds of the children were girls. In Gujarat and Andhra Pradesh, 40 per cent of the children were migrant workers, i.e. children sent from other regions and sometimes even other states to work.¹⁷

Both studies estimated that around 60 per cent of the children never went to school. The other children go to school sporadically outside the farming season, to varying degrees.

As for the use of pesticides, the workers at more than 90 per cent of the visited farms did not have access to suitable personal protection equipment and were not given any training in the safe use of the chemicals. Only two farms were observed to have implemented some basic measures to protect the person who carried out the spraying. It is common for children and adults to be in the field during or immediately after spraying.

5 Information from the company

In June 2011, the Council on Ethics sent a letter to the company asking whether child labour was used in the production of hybrid seed for the company and whether the company had issued any guidelines and implemented measures to prevent this. The company did not respond to the Council's initial request.

A first draft of this recommendation was sent to Zuari in June 2012, in which the company was invited to make any comments it might have.¹⁸ Zuari Global Ltd. responded to this letter in July 2012. The company stressed that no minors were employed by the company and that the company had never employed minors nor encouraged such practice.

The company pointed out that it stipulated strict requirements that the suppliers that produce seed for the company must not use child labour, at the same time as it admitted that any use of child labour that might nevertheless occur may be due to the financial circumstances in this industry. The company further stated that it has repeatedly stressed to the farmers the importance of schooling for children.

The company also pointed out that it does not have any direct control over the individual farmers, that it is the state that has the formal responsibility for ensuring that the law is observed, and that the company's *Code of Conduct* specifies that it does not accept child

¹⁷ This kind of trafficking of children is often organised through a network of agents who pay an advance on the children's wages to the parents against a 10 per cent commission. This system is described in more detail in "Wages of Adolescence: Annual Exodus of Tribal Adolescents from South Rajasthan to Bt Cotton Seed Plots of North Gujarat", Katiyar Sudhir (2006).

¹⁸ Letter from the Council on Ethics to Zuari Industries Ltd., dated 28 June 2012.

labour in its own operations or those of its suppliers, contract producers and other business associates.¹⁹

A renewed draft of this recommendation, with the results from the 2012 surveys, was sent to the company in March 2013. Again, the company was invited to submit any remarks.²⁰ The company maintains that it has not employed children in its production, that the company does not accept the use of child labour in the seed production and the company also informs that it conducts inspections at regular intervals to assure that child labour is not used: “*Contrary to the assertions in your report, neither Company, nor ZSL [Zuari Seeds Ltd.] have employed or encouraged to employ children, as labour, in any form, in its operations. In fact ZSL neither has a concrete link nor a close working relationship with local growers at all. The growing operations are conducted by entering into agreements with Organisers, who in turn identify the local growers. It is pertinent to note that one of the pre-requisites, expressly reflected in each agreement is the “No use of Child Labour in the seed production activities”. The company displays zero tolerance for to the non-compliance to this clause in the agreement. In fact, the representatives of ZSL inspect the farms at regular intervals to ascertain the conformity with the Agreement.*”²¹

6 The Council’s assessment

Introductory observations

The ethical guidelines for the GPFG state that the Council on Ethics can recommend the exclusion of companies from the Fund’s investment universe if there is an unacceptable risk that the company contributes to or is itself responsible for systematic violations of human rights, for example through the use of the worst forms of child labour.

In this case, the Council on Ethics has considered whether the company can be said to contribute to child labour, and if so, whether the child labour in question must be regarded as “*the worst forms of child labour*”. The Council has also considered whether the use of child labour can be considered to be systematic, and whether it is likely that these violations will continue.

Assessment of the extent and nature of the child labour

The Council on Ethics’ surveys indicate that children are estimated to make up around 20 per cent of the workforce involved in production for the company. It is difficult to determine the exact scope of the child labour, and it also varies between different types of seed and different geographical areas, but there are probably somewhere between 3000 and 4000 children working in the production for the company in total.²²

The demonstrated proportion of child labour in production for Zuari corresponds to that found in the Council on Ethics’ previous investigations of other companies that do not have effective measures to reduce the use of child labour. This indicates that the surveys that form

¹⁹ Letter from Zuari Global Ltd. (formerly Zuari Industries Ltd.) to the Council on Ethics, dated 4 July 2012.

²⁰ Letter from the Council on Ethics to Zuari Agro Chemicals Ltd., March 1, 2013.

²¹ Letter from Zuari Agro Chemicals Ltd. to the Council on Ethics, March 19, 2013.

²² This estimate was reached by using the findings concerning the number of children working per unit of land used to produce the different types of seed in the different states and multiplying it by the production area for the different types of seed in the various states.

the basis for this recommendation provide a realistic picture of the conditions in the production of hybrid seed for Zuari.

The Council on Ethics also finds that the proven cases of child labour must be considered to qualify as “*the worst forms of child labour*”. This is supported by several factors.

The young age of the children is one important factor. In the Council on Ethics’ surveys, it was estimated that almost 20 per cent of the children were under the age of 10 years, and 90 per cent of the children were under 14. The majority of the children had no family connection to the production site where the children are involved in seasonal work, and many were working away from their families and care providers.

Another significant factor that makes this case fall under the category “*the worst forms of child labour*” is the obvious health risks that the children are exposed to because of the almost constant exposure to pesticides. Children work without any form of protection in areas during or immediately after spraying. There is widespread, frequent use of pesticides, with crops often being sprayed several times a week. Farms consistently use pesticides that are harmful both on contact with the skin and when inhaled and that can cause serious and permanent health problems with long-term exposure.

The children also have to work very long hours (up to 14 hours a day) and perform demanding physical labour, often in extreme heat. Because the season for the cultivation of hybrid seed is long (at least eight months a year), these children usually receive no or only very limited schooling.

In addition to the fact that the violations specified above are regarded as serious, the Council on Ethics also finds that they must be regarded as systematic and widespread, since children constitute up to 30 per cent of the workforce on the farms included in the studies and on average around 20 per cent.

Link between the company’s operations and the violations

In formal terms, the child labour does not occur at Zuari. The link between the company and child labour is established through the agreements that the company enters into with local farmers. The company enters into agreements with local growers, in some cases through an intermediary, for the production of seed. The company provides inputs such as the seed for planting and pesticides. The company’s representatives inspect the farms at regular intervals to provide advice and guidance and to check the quality and are therefore familiar with the conditions under which production occurs. The Council on Ethics therefore finds that there is an unequivocal link between the company’s operations and the use of child labour in production for the company, and that the company buys seed in full knowledge that extensive use of child labour is common in seed cultivation.

Assessment of the information from the company

The company claims not to control operations on the individual farms. At the same time, the company states that it in fact does conduct regular inspections to ensure that the production is conducted as specified in the contracts, including that child labour is not to be used.

The Council does not know exactly how these inspections are conducted (e.g. how often they are performed and if they are unannounced) or how effective they are, but can only observe that despite of the company’s routines for inspections, extensive child labour is used in the production for the company.

The companies that have succeeded in reducing the use of child labour have implemented concrete programmes to achieve such improvements. The main initiatives have been the introduction of financial incentives where use of child labour is penalised and farmers are rewarded for not using child labour. Parallel to this, monitoring systems have been introduced with unannounced inspections.

The fact that a company has a *policy* or *code of conduct* is not sufficient in itself to achieve reductions in the use of child labour. Nor is it sufficient that the company has established control mechanisms if these are not suited to detect instances of child labour. As long as the company does not introduce more appropriate measures to mitigate the problem, it is likely that child labour will be used in production for Zuari in the future too.

Assessment of future risk

There does not seem to have been any significant reduction in the use of child labour in production for the company from 2011 to 2012. The results are not directly comparable, since the working conditions have been studied in connection with the cultivation of different types of seeds. To the extent that there can be said to have been a slight decrease in the scope of child labour (compared with the figures from the production of cottonseed), it is probably due to other factors, such as a poor harvest, rather than measures implemented by the company. The Council on Ethics therefore finds no grounds to believe that there is a downward trend in the use of child labour in production for the company.

In the light of these factors, the Council on Ethics finds there is an unacceptable risk that the company contributes to systematic use of the worst forms of child labour and that this will continue in the future.

7 Recommendation

The Council on Ethics recommends that the company Zuari Agro Chemicals Ltd. be excluded from the investment universe of the Government Pension Fund Global due to an unacceptable risk that the company contributes to serious, systematic human rights violations.

Ola Mestad
Chair

(sign.)

Dag Olav Hessen

(sign.)

Ylva Lindberg

(sign.)

Marianne Olsson

(sign.)

Bente Rathe

(sign.)