Responsible disengagement: preventing '*cut and run*' through the EU Corporate Sustainability Due Diligence Directive

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Recommendations

The Omnibus proposal reinforces the economic insecurity for business partners at risk of disengagement and could have significant adverse impacts on livelihoods of small business operators. We recommend members of the European Parliament to form compromise amendments that:

1. Ensure suspension is always temporary and time-bound, to ensure companies in scope do not use this approach to put undue pressure on their business partners, in particular SMEs and smallholders, without any intent to address adverse impacts;
2. Keep termination as a last resort measure;
3. Require meaningful stakeholder engagement prior to disengagement (in Article 13 CSDDD).

Introduction

Small and self-employed businesses contribute substantially to global supply chains. For example, 600 million smallholder farmers worldwide produce 46% of the world's food on just one-third of the world's agricultural land. In the EU, SMEs make up 99.5% of the textile sector, supporting local economies in Italy, Romania, and Bulgaria. Yet, these small operators often lack the conditions to produce their goods and services in an economically, socially, and environmentally sustainable way. Many smallholder farmers rarely earn a living income, and when they hire workers, they often are unable to pay them a living wage. Similarly, SMEs are often pressured into short-term contracts that push them into a race to the bottom to remain competitive.

Experience shows that instead of supporting these small suppliers, downstream companies are often risk-averse and "cut-and-run" - i.e. they disengage from them prematurely, without attempting to use their leverage to change practices. In fact, standard contracts, imposed on suppliers, often even allow buyers to exit, without needing to mitigate the negative impact of disengagement. In addition, buyers often engage in unfair purchasing practices, such as unilateral contract changes and order cancellations. Suppliers are therefore left in vulnerable situations.

This jeopardises small businesses' economic sustainability and livelihoods and only further reinforces the vicious circle leading to more human rights violations and environmental harm.
The EU Corporate Sustainability Due Diligence Directive (CSDDD) can be a powerful instrument to protect small and self-employed businesses, through clear provisions safeguarding against cut-and-run. Limiting disengagement as a last resort and ensuring it is conducted responsibly, in consultation with

affected stakeholders, is therefore key to strengthening supplier resilience to external risks and ultimately to enhance companies' competitiveness.

Impact of cut-and-run

"Cut-and-run" directly undermines progress toward living wages and living incomes, which are rights firmly enshrined in the International Covenant on Economic, Social and Cultural Rights. Abrupt order cancellations or exits trigger liquidity shocks for suppliers, which translate into unpaid wages and even job losses with unpaid severance. The constant threat of disengagement also indirectly weakens workers' bargaining power due to fears of related lay offs, keeping wages stuck below living wage benchmarks. For smallholders, losing a buyer removes sales volume needed to achieve a living income. Households often respond by cutting essential spending, taking on high-cost debt, shifting to lower-value or less regulated markets, or selling their goods at a price below the production costs. These pressures can further aggravate human rights violations and environmental harm as families and small businesses scramble for replacement income – e.g. resorting to child labour instead of hiring workforce, or deforesting in the hope to increase yields. Cut and run therefore directly undermines the objectives of the CSDDD.

It also has a significant macro-economic impact: in Bangladesh, buyers exiting irresponsibly during the COVID-19 pandemic in spring to autumn 2020 led to about US$3.16-3.8 billion in orders canceled or suspended, with approximately 1150 factories and 2.28 million workers impacted. The Fair Trade Advocacy Office and Clean Clothes Campaign conducted research on the impact of such terminations in the EU and documented the devastating impact on key economic sectors in Bulgaria, Romania, Croatia, the Czech Republic, Italy and Germany.

Case study 1: Disengagement leading to brutal shifts in employment and supply chain organisation – forced labour cases in the shrimp sector in Thailand

Following several reports in 2014 to 2016 linking Thai shrimp supply chains to forced labour, several Western retailers suspended purchases (e.g. Carrefour suspended orders from CP Foods), and major exporters such as Thai Union rapidly ended all subcontracting to external shrimp "peeling sheds". This disengagement delivered a sudden demand shock to micro-SMEs at the pre-processing tier, and reports estimate that 5000 workers lost work overnight. This shows how abrupt disengagement without prior due diligence or a responsible exit strategy can shift the costs of addressing risks onto the actors with least capacity to address them.

Preventing irresponsible disengagement in due diligence

Rather than a 'tick-the-box' exercise, due diligence must be applied as a dynamic and collaborative process, one that results in ever-improving human rights and environmental standards. It requires a shift to long-term purchasing commitments, and that companies take all appropriate measures - including meaningful engagement, support for remediation, alignment of purchasing practices, and the use of leverage - to prevent or mitigate adverse impacts.

The OECD Guidelines for Multinational Enterprises on Responsible Business Conduct, which currently set the authoritative voluntary standard on due diligence, define the different stages of actions to be taken by companies regarding their business relationships while mitigating adverse impacts:

1. Continue the relationship throughout the course of risk mitigation efforts;

2. Temporarily suspend the relationship while pursuing ongoing risk mitigation;
3. or, as a last resort, disengage from a business relationship either after failed attempts at mitigation, or where the enterprise deems mitigation not feasible, or because of the severity of the adverse impact.

The OECD Guidelines emphasise that, when it is possible to demonstrate a realistic prospect of, or actual improvement over time, maintaining the business relationship will often be preferable to disengagement. Companies are also advised to '*take into account potential social, environmental and economic adverse impacts related to the decision to disengage*'. When disengagement is inevitable, companies should disengage '*responsibly including by seeking meaningful consultation with relevant stakeholders in a timely manner and where possible, by taking reasonable and appropriate measures to prevent or mitigate adverse impacts related to their disengagement.*'

Responsible disengagement and preventing cut-and-run is a key component of due diligence and essential to ensuring that companies themselves take steps to uphold human rights and environmental standards rather than passing the burden onto their suppliers. However, without binding legislation on the matter, this aspect in particular has been poorly implemented. The Fashion Revolution 2023 Transparency Index shows that only 24% of global brands disclose their responsible exit strategy when leaving a supplier. Yet, it is possible to improve on this: In the apparel sector in China, almost 80% of brands disclose responsible exit policies (SOMO 2024) - and the CSDDD is cited as an explicit reason by companies surveyed.

There is therefore a strong need to regulate disengagement as part of the due diligence obligation, to ensure the CSDDD does not lead unintendedly to an increase of disengagement as an easy and cheap mitigation measure. It is essential to protecting small and self-employed businesses.

The CSDDD provisions

The CSDDD as adopted in 2024 regulates well how companies in scope should disengage. Recital 32 outlines that the directive "*should ensure that disengagement is a last-resort action*" to "*enable continuous engagement with the value chain business partner instead of termination of business relations (disengagement) and possibly exacerbating adverse impacts*".

It clearly lays out in articles 10 and 11 the last resort character of disengagement, as well as a sequence of actions companies must take:

1. First, adopt and implement an enhanced prevention or corrective action plan, including by using or increasing the company's leverage through the temporary suspension of business relationships;
2. If there is no reasonable expectation that the company's efforts will succeed, disengage.

The CSDDD also states that, prior to temporarily suspending or terminating a business relationship, the company shall assess whether the adverse impacts from doing so can be reasonably expected to be manifestly more severe than the adverse impact that could not be prevented or adequately mitigated. Should that be the case, the company shall not be required to suspend or to terminate the business relationship, and shall be in a position to report to the competent supervisory authority about the duly justified reasons for such decision. Further, Article 13 requires companies to engage with stakeholders when deciding to terminate or suspend a business relationship. This ensures that, when assessing

whether the adverse impact would be more severe in case of disengagement, the company takes into account stakeholders' input in line with the "do not harm" principle. Without this obligation, the livelihoods of SME business owners and their own suppliers could be jeopardised.

The Omnibus proposal

The Omnibus proposal removes the obligation laid out in articles 10 and 11 to disengage responsibly as a last resort and to require engagement with stakeholders prior to suspension and termination. This breaks down into two significant issues:

1. It only refers to suspension, without ensuring such suspension would be time bound - so it could de facto result in termination. The proposal therefore maintains the current status quo - the possibility for major companies to arbitrarily cut and run without compensating for the consequences - by not putting in place safeguards to prevent harmful economic impacts for suppliers.
2. This article is coupled with the proposal in Article 4(7) to remove the obligation for stakeholder consultation during disengagement. This would make it impossible for smallholders, workers or suppliers to have mechanisms to voice their concerns about the adverse consequences of termination or even suspension of contracts with their buyers.

Case study 2: Irresponsible suspension in Guatemala – child labour cases in coffee production

An investigation alleged that two major coffee companies, 'X' and 'Y', are being supplied by a supplier which has children (some as young as 8) working on coffee farms in Guatemala. Upon these allegations, the companies faced reputational and legal pressure to act swiftly. Company X's response was to immediately suspend all purchases from the implicated region. The CEO of Company Y announced they would stop all purchases of coffee from all farms in the region, pending investigation, and would not resume until assured no child labour is present, and the other company took similar action.

The response did not include support measures for the affected farmers in addressing the issue. All smallholder farmers – even those who were not part of the investigation - suddenly lost a key buyer. For local coffee farmers, the corporate reaction meant an instant loss of income. Cooperative leaders noted that smallholders who had depended on those export contracts were left in limbo. This falls short of "responsible disengagement," which would require companies to mitigate the negative impact on the smallholder's livelihoods. While suspension can be a legitimate tool to exert leverage in response to human rights violations, responsible disengagement must involve a clear time-bound plan accompanied by adequate support measures to ensure this leads to positive results, rather than inadvertently reinforcing the root causes of violations.

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