

Palm Oil Action Plan

PROGRESS REPORT 2016



July 2017



performance
WITH purpose



Introduction

In 2006, PepsiCo launched Performance with Purpose, our vision to deliver top-tier financial performance over the long term by integrating sustainability into our business strategy. Our focus includes transforming our portfolio and offering healthier options while making our food system more sustainable and communities more prosperous. In doing so, we believe we will pave the way for PepsiCo's future growth and help others thrive.

Fundamental to our vision is a commitment to source our food and beverage ingredients in a way that respects the natural environment and promotes human rights. Through our Sustainable Farming Initiative, we work with farmers in our global supply chain to incorporate industry-leading policies, practices and technologies that can make our food system more sustainable and productive.

Palm oil is a key area of focus. PepsiCo is a significant buyer of palm oil and, as a result, has a complex global supply chain that encompasses dozens of suppliers, more than 1,500 mills and tens of thousands of farms and plantations that produce palm fruit. We recognize and share the concerns of our stakeholders about the environmental and human rights issues that persist in some parts of the palm oil industry, particularly in Indonesia and Malaysia, the world's largest producers.

In 2015, PepsiCo launched its Palm Oil Action Plan, committing to help advance the sustainability of the palm oil industry. We published our first Annual Progress Report in 2016. That same year, we reiterated our specific commitment to source 100 percent certified sustainable palm oil as part of a new, broader set of sustainable sourcing goals under our Performance with Purpose 2025 Agenda.

This year, our second Annual Progress Report provides detailed information on the strides we are making toward our goals. It covers all of the commitments in our 2015 Palm Oil Action Plan, which we have included in the appendix. We have organized this report into the following sections:

- I. **Our progress:** a summary of the aspects of our action plan where we have achieved the greatest progress and an overview of what we have learned;
- II. **Our approach and policy:** the role that palm oil plays in our business and the policies and commitments to which we hold ourselves and our suppliers accountable;
- III. **Traceability:** our efforts to achieve greater visibility into all aspects of our palm oil supply chain, from direct suppliers to mills to farms and plantations;
- IV. **Risk assessment and prioritization:** identification of the key areas of our supply chain that need the most immediate attention;
- V. **Actions to drive change:** our efforts in the short, medium and long term to use our influence in ways that encourage progress across the palm oil sector, including certification, direct supplier engagement and support for producers;
- VI. **Addressing claims of non-conformance with our policies:** a description of how we address environmental and social complaints related to our palm oil supply chain in order to uphold our policies and achieve positive outcomes;
- VII. **Transparency and stakeholder engagement:** our commitment to providing regular updates on our progress and the engagements we have undertaken to shape and inform our approach; and
- VIII. **Next steps:** our top priorities in 2017 as we strive to meet our commitments.

We welcome comments or questions about this report; please contact us at SustAg@PepsiCo.com.

I. Our progress

We consider the following developments to best illustrate the progress we have made over the last year toward meeting our palm oil commitments and addressing the challenges that remain:

- PepsiCo significantly improved visibility into our global palm oil supply chain. We made further progress on traceability to the mill level, now up to 89 percent, and implemented leading practices that will help increase transparency and accelerate the uptake of traceability systems across the industry. Based on the improved data, we completed a review of environmental and human rights risks. Data collection capability among suppliers needs further development, but we are confident it will improve. At the same time, we are investing in third-party verification to enhance data quality.
- For visibility to farms/plantations, a common industry definition on traceability is currently lacking, so we began collaborating with industry and other stakeholders to address this gap.
- We established a process of proactive engagement with all direct suppliers. In addition, we are developing a new supplier scorecard with emphasis on policy, engagement, certification and grievances. This work has provided us with better insights into the risk of non-conformance with our environmental and human rights policies. It has also improved our ability to prioritize how we mitigate that risk through supplier engagement and investment in positive impact programs, which we can now accelerate.
- We developed a grievance mechanism for dealing with environmental and social complaints involving palm oil and other agricultural raw materials in our supply chain. Our aim is to uphold our policies and achieve positive outcomes, and among food and beverage companies, we believe our mechanism is leading practice. Consistent with our commitment to the UN Guiding Principles on Business and Human Rights, we have sought to use our relationships to bring resolution to palm oil complaints involving our supply chain, including and beyond our direct suppliers.
- In 2016, we increased our procurement of physically certified sustainable palm oil to 16 percent of our volume, using the Roundtable for Sustainable Palm Oil (RSPO) standard, and we are targeting 30 percent by the end of 2017. In some local markets, physically certified supply is not currently available, and greater investment in capacity building is required.
- We began a process to invest in the improvement of conditions in key sourcing regions, including Indonesia and Mexico. For example, we are sponsoring the National Interpretation of the RSPO Principles and Criteria in Mexico while supporting a program that will provide training on High Conservation Value (HCV) and High Carbon Stock (HCS) assessments.
- We expanded our stakeholder engagement to include broader interaction with civil society organizations and industry platforms. For example, we participated in a palm oil workshop hosted by Oxfam, helped lead palm oil traceability webinars under the auspices of the Consumer Goods Forum, and joined the Tropical Forest Alliance (TFA) 2020 Partnership. Though a number of strong platforms for collaboration exist, more effort is needed to drive improvement at scale, especially in regions where environmental and human rights issues are systemic, persistent across a broad landscape, and exacerbated by federal and local regulations that may not be sufficient or applied consistently.
- We are proud of our progress in 2016 but know that more is required. Through our extensive engagement, we have heard specific points of criticism about the need to move farther and faster. We are, however, encouraged by acknowledgement of our progress. In 2016, for example, our Palm Oil Action Plan was evaluated by the World Wildlife Fund in a global ranking of consumer goods companies, and PepsiCo was recognized for leading the way on progress on essential actions on sustainable palm oil.

II. Our approach and policy

Key points in this section:

- We have a comprehensive set of policies and commitments to promote the environmental and social sustainability of our global palm oil supply chain.
- We seek to use our role to catalyze broader action and raise standards across the sector.

Palm oil is the most widely used edible oil in the world¹ and an ingredient in a variety of PepsiCo food products. Like many of our stakeholders, though, PepsiCo has ongoing concerns about how some palm oil is produced. Rainforest conversion, biodiversity loss and human rights abuses persist in various producing regions. Through our policies and actions, PepsiCo seeks to support the growth of sustainable palm oil, first by

Box 1: Why palm oil production is growing

“Oil palm trees are incredibly efficient, yielding more oil on the same amount of land than any other leading oil crop – four to ten times more than soy, rapeseed (canola), or sunflower.

Palm and palm kernel oil are incredibly versatile. Their many uses range from cooking oil and shortening, to specialized blends and ingredients that can be found in about half of all packaged products – snacks and baked goods, frozen foods, soaps and detergents, even toothpaste. Palm oil is also increasingly used as feedstock for biofuels.

When you consider this crop efficiency and versatility, combined with a relatively low cost of production, it’s no surprise that global demand for palm oil has more than doubled [from 2005 to 2015]. This exceptional growth has brought economic and employment benefits for millions of growers, but it has also brought unprecedented threats to forests, wildlife, and people where oil palm is grown and harvested.

For this reason, companies, NGOs, governments, and other stakeholders are working together to move the entire palm oil sector toward a more sustainable future.”

- Conservation International & World Wildlife Fund; *Sustainable Sourcing Guide for Palm Oil Users: A practical handbook for US consumer goods and retail companies*; May 2015.

addressing standards in our own supply chain and then by partnering with others to drive improvement more widely. In this way, we hope that our collective actions will improve palm oil production across the industry, reducing the harm that may be done, while expanding the benefits (Box 1).

PepsiCo is a significant buyer of palm oil, which we use primarily in snack manufacturing because it is relatively stable and readily sourced in some regions. In the United States, we use almost no palm oil, but it is used in Asia and other markets. In 2016, our global purchase of palm oil was roughly 480,000 metric tonnes (MT) of which palm kernel oil comprised about 4,600 MT. Our top three suppliers were Cargill, Oleofinos and Wilmar, and the

top three countries from which PepsiCo sourced palm oil were Indonesia, Malaysia and Mexico.

Despite being a buyer of palm oil, our purchase in 2016 represented less than 0.8 percent of the global supply. The market for palm oil is highly fragmented, and the majority of palm oil does not receive sustainability certification. This means that, in order to meet our sustainable palm oil goal, we must strive to use our position in the global supply chain to promote industry-wide collaboration and action at scale to promote a sustainable future for the entire sector.

Our policies and commitments (see Appendix for details) apply to the sourcing of palm oil for all PepsiCo brands and products worldwide. This includes our commitments to eliminate deforestation and human rights abuses from our palm oil supply chain. We believe that fulfilment of these policies and commitments will make

¹ US Department of Agriculture, Oil Crops Yearbook, <https://www.ers.usda.gov/data-products/oil-crops-yearbook>

our supply chain more secure and support stable social, economic and environmental conditions for producers, mills and the communities they support.

We have a related commitment to addressing climate change. We support the Paris Climate Accord and have an ambitious science-based goal to reduce absolute greenhouse gas emissions by at least 20 percent across our value chain by 2030. To achieve this goal, we must reduce emissions in our agricultural supply chain, including palm oil, by working to eliminate deforestation and loss of peatlands.

Engagement is an important part of our approach and helps to guide our actions. We meet directly with stakeholders on palm oil on a frequent basis and welcome the opportunity to listen to their concerns, receive input and advice about our programs, and explain our approach to support the development of a sustainable palm industry. Given the impacts associated with some palm oil cultivation, we understand that stakeholders want PepsiCo to move as fast as possible, which is why we have developed a dedicated, cross-functional, global team with deep expertise to execute our Palm Oil Action Plan and accelerate progress toward achieving our commitments.

For additional related information, please see the following PepsiCo documents and related links:

- [Palm Oil Commitments, 2015](#)
- [Palm Oil Action Plan, 2015](#)
- [Palm Oil Traceability Protocol](#)
- [RSPO Annual Communication of Progress \(ACOP\)](#)
- [Global Human Rights and Salient Issues Statement](#)
- [Forestry Stewardship Policy](#)
- [Land Use Policy](#)
- [Performance with Purpose 2025 Agenda](#)

III. Traceability

Key points in this section:

- In 2016, PepsiCo had 60 direct palm oil suppliers around the world, supplied by more than 1,500 mills, which collectively rely on tens of thousands of producers ranging from large plantations to individual smallholders.
- We have made strong progress toward our goal of 100 percent traceability to the mill. As of July 2017, we estimate that approximately 89 percent of the palm oil we will use during 2017 has been traced to specific mills, up from 65 percent in 2015.
- Building on our Palm Oil Traceability Protocol, we are now focused on third-party verification of data as well as industry collaboration to promote traceability and interoperability of systems.
- We are also collaborating with industry and other stakeholders to align on a common definition of farm/plantation traceability; we committed to achieve farm/plantation traceability by 2020.

Supply chains can be long and complex, often involving multiple tiers of suppliers and ultimately thousands of actors. To ensure that our policies are being met, improve standards and drive positive impact on the ground, we must know where our palm oil comes from. Building better information systems is therefore a critical step to achieving our goals.

We committed to mapping our palm oil supply chain to the mill level by the end of 2016. To ensure the quality and consistency of the data we receive from direct suppliers, PepsiCo worked with Control Union and

Proforest to develop and implement PepsiCo's Palm Oil Traceability Protocol. The Protocol was distributed to all direct suppliers in 2016 together with a recommended quarterly reporting template, which requires the names of all palm oil and palm kernel oil mills, their GPS coordinates and the percentage of PepsiCo's volume that is traceable to the mills. A training program was implemented in English and Spanish for our direct suppliers on how to use the Protocol, and we established a traceability helpdesk with Control Union to provide ongoing assistance, all of which helps ensure timely, accurate data. The [Protocol](#) is available to the public.



Thanks to these efforts and the diligence and partnership of our direct suppliers, we have good visibility to where the mills are based. Ninety-eight percent of our direct suppliers have reported data to PepsiCo. Based on that data, as of July 2017 we estimate that approximately 89 percent of the palm oil we are forecasted to use for the year has been traced to specific mills, up from 65 percent as reported in 2015.

We have data on the remaining percentage of mills but believe that the quality is not yet sufficient to meet the high bar we have set for traceability. For example, a missing GPS coordinate would preclude a mill from being "traceable." We have been challenged by the ability of some suppliers to provide timely, complete data coupled with the complexity of the supply chain. We continue to work with suppliers to improve their awareness and understanding. For example, we have developed a quarterly traceability progress score on suppliers to track how they are doing, and we focus additional engagement where it is needed. Through these efforts we will continue to increase the visibility of the mills in our palm oil supply chain with the aim of 100 percent traceability.

To promote greater transparency in the palm oil sector, PepsiCo helped lead two industry webinars under the auspices of the Consumer Goods Forum, a network of global retailers, manufacturers and service providers. These webinars focused on traceability and included participation and perspectives from Unilever, Cargill, the IDH Sustainable Trade Initiative and others. In addition to presenting our experience and learning on traceability, PepsiCo's objective was to promote interoperability of data systems, which should help to accelerate traceability across the industry.

The next step in our mill traceability work is to initiate third-party verification of the data, adding an independent view on its accuracy and credibility. As described in our Palm Oil Traceability Protocol, all direct suppliers will be required to have an independent third-party review of the data that is sent to PepsiCo. In cases where the data may need improvement, then we may go further to include upstream data audits of indirect suppliers. By taking this step, we believe we would be helping to lead the industry on establishing and potentially converging around data systems.

Mapping of the mills provides the basis for extending our traceability work to palm oil farms/plantations, which number in the tens of thousands in our supply chain. We have committed to do this by 2020 and have already started work in parallel to mill traceability. We are collaborating with others in the industry, such as the IDH-led Landscape Working Group, to align around a common definition for farm/plantation traceability. This will be incorporated into our Palm Oil Traceability Protocol and supplier engagement program. Some of our suppliers are already working on this mapping challenge independently. We will collaborate and support these efforts, and we will give particular attention to smallholder farmers for which information is difficult to obtain.

Lastly, because palm oil is processed into a diverse array of derivatives, PepsiCo also committed to asking our suppliers to identify the use of palm oil derivatives in our ingredients. We initiated a dialogue with suppliers starting in 2015. Based on these discussions and analysis, we believe that the volumes are very low, likely to be

less than 1 percent of PepsiCo's global palm oil use. In light of this, our focus will remain where we have the most impact, specifically the procurement of palm oil and palm kernel oil.

IV. Risk assessment and prioritization

Key points in this section:

- PepsiCo completed a review of environmental and human rights risks across our palm oil supply chains, using improved data from our traceability program.
- We are seeking to bring new investment to improve conditions in Indonesia while laying the foundation for new capacity for sustainable palm oil in Mexico.

Risk assessment provides PepsiCo with insights that allow us to guide resources to where they are most needed. Our risk assessment process employs mill traceability data, mill visits and related information to systematically identify high-risk palm oil suppliers and production regions and then prioritize our actions and investments, which supports conformance with our policies and guides investment in positive impact programs. In addition, direct suppliers who have gone through our Business Continuity Planning are subject to PepsiCo's third-party audit program for our Supplier Code of Conduct, known as the Sustainable Sourcing Program.

PepsiCo's palm oil supply chain is global. We have supply from established, leading production regions such as Indonesia and Malaysia as well as newer production regions in Latin America. Consequently, we are evaluating risks ranging from legacy issues to potential prospective deforestation and human rights threats that are yet to materialize. Against that backdrop, our proximity to the palm oil mill and plantation—both in terms of the length of the supply chain and, to a lesser extent, geography—shapes the extent of our influence to address potential problems and drive change on the ground.

In 2016, we used the data collected on mill traceability to complete a review of all direct suppliers and identified priority areas for engagement. We also began work to develop country-specific risk profiles starting with our largest sources of supply. As PepsiCo implements its risk assessment process, we believe that environmental and human rights issues are systemic in some regions. Adding to the challenge are inconsistent federal and local regulations that vary from place to place. As a result of these factors, broad industry collaboration and investment is required, but coordination on such a broad level requires new mechanisms, improved institutions and greater capacity than currently exists. We need more solutions and solution providers to support change at scale.

With respect to Indonesia, a key sourcing region where significant environmental and human rights issues have been reported, our risk review included extensive discussions with direct suppliers, and we determined that the pattern of risks across Indonesia—including labor rights, deforestation, peat loss and smallholder inclusion—has been effectively characterized by the suppliers themselves as well as other stakeholders such as NGOs. Consequently, we decided that rather than undertaking mill visits that would confirm what is already known, we should move directly to evaluation of impact programs—a priority focus for 2017—which we believe is the best use of time and resources. For example, an impact program could be working with smallholders to improve their production and achieve certification. We have contacted a variety of stakeholders, including suppliers and civil society organizations, and communicated our intent to collaborate and bring new investment to one or more programs in Southeast Asia.

In Latin America, where palm oil production is increasing, three mill assessments were conducted in the second half of 2016, one each in Mexico, Colombia and Honduras, respectively. The work was led by Proforest

and done in collaboration with our direct suppliers, building on their relationships with the mills. A protocol for these visits was developed based on a checklist constructed by the Traceability Working Group, a project coordinated by the IDH Sustainable Trade Initiative. This checklist has been developed with input from a wide range of companies and other stakeholders and provides a template that should facilitate sharing of information and results. The mill visits identified various areas needing further improvement and support, including: 1) implementation of HCV/HCS identification, management and monitoring to ensure no deforestation, 2) health and safety conditions for workers and subcontractors, and 3) proper management and disposal of effluents, waste and by-products.

Lastly, as part of a series of studies undertaken in response to human rights concerns raised by Oxfam, PepsiCo funded an assessment of "[Land tenure and other human rights issues in the oil palm and sugarcane sectors in Mexico](#)," which we have published in 2017. The assessment was led by Proforest in consultation with key stakeholders, including Oxfam, and presents the findings of an analysis of land rights, labor rights, community impacts, transparency and other human rights risks in Mexican oil palm and sugar cane supply chains. Though it is not a comprehensive human rights assessment of the sectors or specific suppliers, the report is designed to inform PepsiCo and other actors in the palm oil supply chain on opportunities to address barriers to sustainable production in accordance with RSPO standards. PepsiCo will work with RSPO and other supply chain actors to communicate these opportunities and support development of a platform for continuous improvement in Mexico.

V. Action to drive change

Key points in this section:

- In 2016, our ramp up of physically certified palm oil reached 16 percent of our volume as compared to 8 percent in 2015, and we are targeting 30 percent by the end of 2017.
- We are sponsoring the National Interpretation of the RSPO Principles and Criteria in Mexico and providing support to increase awareness of sustainable palm oil production, including training on High Conservation Value (HCV) and High Carbon Stock (HCS) assessments.
- We are developing a new scorecard for direct suppliers with emphasis on policy, engagement, certification and grievances.

PepsiCo is a significant buyer of palm oil and yet our consumption represents less than 0.8 percent of global production. In light of this, we recognize that we have a responsibility to lead in driving the development of a sustainable palm oil industry, but lasting change will require action across the sector. We use our position in the supply chain to encourage and support our direct and indirect suppliers to adopt sustainable practices. In doing so, we aim to play an active role in a wider transformation. When we set out our Palm Oil Action Plan in 2015, we envisioned a long-term path that would make significant use of industry collaboration (Figure 1).

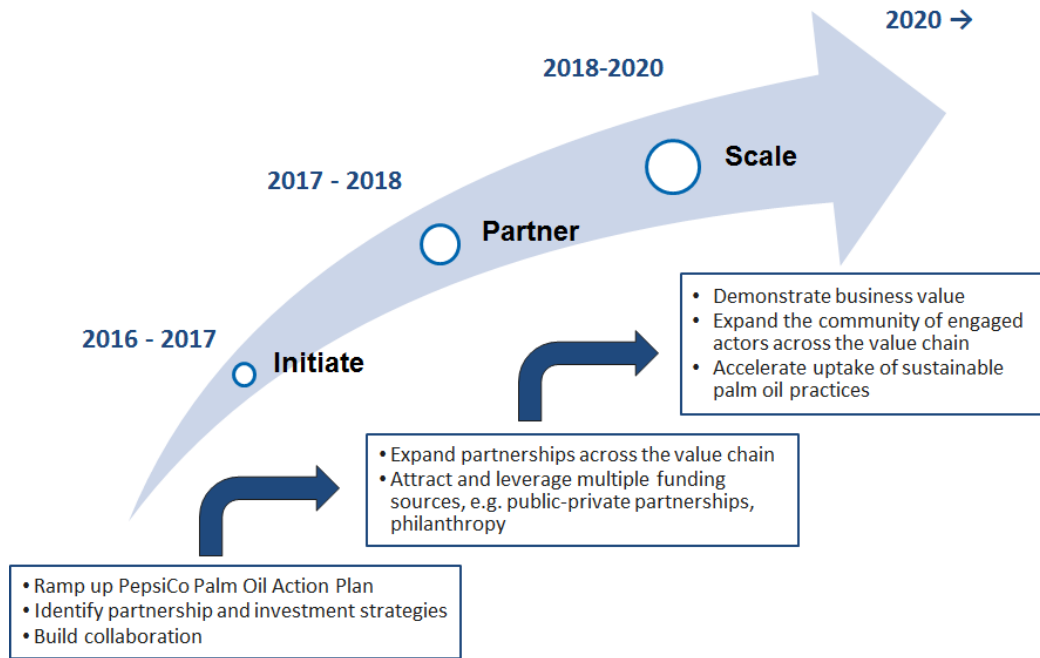
Roundtable on Sustainable Palm Oil (RSPO) Certification

RSPO is a not-for-profit body that draws membership from across the palm oil sector, from producers to buyers. Its environmental and social criteria are the most widely accepted standard for certified sustainable palm oil.

Since joining in 2009, PepsiCo has supported RSPO and actively worked with our suppliers to promote the benefits of membership, including benefits to the environment, workers, local communities and business. We also support RSPO Next, an advanced certification scheme that incorporates additional protections for forests, peatlands and human rights. Our Palm Oil Commitments and Action Plan are aligned with the direction of

RSPO Next, and we look forward to engaging with RSPO’s 2018 Principles & Criteria consultation. Additionally, PepsiCo has begun work on our Chain of Custody Certification for palm oil, including the completion of a pilot market exercise this year. This is a necessary step for our certification claims to be supported by RSPO.

Figure 1: PepsiCo’s theory of change: Initiate, Partner, Scale



Ninety-three percent of our direct suppliers were RSPO members at the end of 2016, accounting for approximately 98 percent of our forecasted direct palm oil volume. The unique exceptions were suppliers in Venezuela, where local political and economic volatility presented unusual challenges to membership. We continue to work to have all direct suppliers join RSPO as members.

PepsiCo has a commitment to 100 percent RSPO certified sustainable palm oil supply, which we first achieved in 2015 by relying primarily on Green Palm Certificates (now RSPO Credits). This system offered a means for RSPO certified palm oil buyers to support the development of the sustainable palm oil sector, but it has not provided the necessary level of supply chain transparency. So, in 2015, PepsiCo took the next step by committing to switch to physical certification, or 100 percent physically certified RSPO sustainable palm oil, by 2020. Certification may not guarantee that our policies are being met throughout our supply chain, but it is a vital part of industry-wide efforts to raise the bar for performance across the industry.

We are making progress toward this target, and we recognize the need to do more. In 2016, PepsiCo doubled our use of mass balance physically certified palm oil to 16 percent of our volume as compared to 8 percent in 2015, and we are targeting 30 percent by the end of 2017. For the remainder of our palm oil use in 2016, we relied on Green Palm certification, which has now transitioned to RSPO Credits.

Capacity-building and smallholder certification

We know that some of our stakeholders expect us to move faster in the shift to physical certification, and we have developed a roadmap to 2020 to accelerate our progress and achieve our goal. In certain local markets, volumes of physically certified RSPO sustainable palm oil are not available in sufficient quantities and require investment in capacity building and support from both local and international actors.

We are also committed to support the inclusion of smallholders. Given that 40 percent of the world's palm oil is produced by smallholders², their participation in the shift to sustainable palm is critically important and requires industry-wide initiatives and collaboration, especially in the largest and most fragmented production markets, such as Indonesia. In smaller, newer production markets where PepsiCo may have the advantage of scale, we have additional opportunities to lead the shift to sustainable palm.

A visible example of our approach involves Latin America, where we source significant volumes but RSPO is not well established. We sponsored the National Interpretation of the RSPO Principles and Criteria in Mexico and are working with our suppliers and other actors across this growing production region to increase capabilities. Working in partnership with Proforest and Mexico's palm oil industry association, FEMEXPALMA, we have developed a program that starts with improving local capabilities among small, medium and large producers to identify, manage and monitor HCV ecosystems. The next step will be a regional HCV and HCS assessment conducted across a 52,000 hectare landscape that spans six palm oil producing regions in Tabasco and Chiapas.

Working with smallholder farmers can be challenging. Many are in traditional and hard-to-reach rural communities and lack access to training or infrastructure. PepsiCo is developing long-term programs in collaboration with our direct suppliers and other stakeholders to support smallholders, including addressing risks of deforestation and human rights abuses. Most recently, PepsiCo submitted a grant proposal to the RSPO Smallholders Support Program for sustainable palm oil in Mexico. After review, we were asked to make adjustments and resubmit in the second half of 2017, which we are doing. The objective is for Mexican smallholders to achieve RSPO independent group certification while contributing to their livelihoods and ensuring the sustainable supply of certified palm oil. We are evaluating similar programs to support smallholders in other producing regions, and we look to include direct and indirect suppliers in these efforts.

Engaging direct suppliers

Through sustained, consistent engagement, our objective is for all direct suppliers to understand and help deliver on PepsiCo's policies and commitments. This includes ensuring that all suppliers know our Supplier Code of Conduct, which clarifies our global expectations in the areas of labor practices, associate health and safety, environmental management and business integrity, while encouraging suppliers to adopt high standards for palm oil sustainability.

PepsiCo's practice is to incorporate our Supplier Code of Conduct in palm oil contracts and purchase orders, and suppliers have access to a training module on our website (www.pepsico.com/purpose/responsible-sourcing). Also, as part of our Performance with Purpose 2025 Agenda, we expanded our Sustainable Sourcing Program (SSP). This program assesses risk and monitors supplier compliance with our Supplier Code of Conduct through third-party auditing of our most business-critical direct suppliers, contract manufacturing and co-packing locations across 68 countries. Suppliers are responsible for demonstrating compliance with PepsiCo's expectations through activities that include completion of Supplier Code of Conduct training, scored site-level Self-Assessment Questionnaires, and participation in on-site audits, as required, based on the Sedex Members Ethical Trade Audit (SMETA) 4-Pillar protocol. When non-compliance is found during an on-site audit, a corrective action plan with a timeline for remediation is put in place by the supplier site and verification of closure is conducted through a follow-up review by an approved third party auditing firm. In 2016, 62 percent of our direct suppliers of palm oil completed SSP Supplier Code of Conduct training, and 15 on-site audits were conducted or recognized with no critical areas of noncompliance.

In addition, we continue our diligence to include in all new PepsiCo contracts for the direct procurement of palm oil a specific reference to PepsiCo's Forestry Stewardship and Land Use Policies and the principles contained within PepsiCo's Palm Oil Commitments, which will require that a supplier not knowingly source

² RSPO, <http://www.rspo.org/smallholders>

material in violation of these policies and develop and maintain a process to ensure that its supply chain is informed of and adheres to similar principles. The supplier also agrees to report at least annually on this process to PepsiCo.

In 2016, PepsiCo shared our Palm Oil Action Plan with all of our direct suppliers. This included the requirement that they must be members of RSPO. We also began implementation of our Palm Oil Traceability Protocol, as discussed in Section III. This substantially deepened our relationships and positive interactions with direct suppliers, which in turn has opened up avenues for vital industry collaboration, including action and effort on the part of indirect suppliers. We also meet regularly with suppliers at events such as the 2016 RSPO Roundtable in Bangkok and during targeted in-person meetings to advance our collective agenda.

As our engagement with direct suppliers has expanded, we are developing a palm oil supplier scorecard that is being implemented during 2017. The scorecard includes the following four key areas:

1. Policy, including human rights and land use policies in place,
2. Engagement, including time-bound engagement plans, grievance mechanisms in place, and public progress reporting,
3. Certification, including RSPO membership and chain of custody certification, and
4. Grievances, including known grievances in the supply chain and steps being taken to address them.

Lastly, in 2016 PepsiCo requested our direct suppliers of palm oil to report their greenhouse gas (GHG) emissions through the CDP Supply Chain platform. Many of our large international suppliers completed one or more of the reporting modules offered by CDP, accounting for about one quarter of our palm oil supply volume in aggregate. However, we have found that the majority of our suppliers, particularly smaller national or regional companies, did not use the platform, most likely owing to the extensive nature of CDP reporting. Going forward, we will continue to encourage suppliers to report their GHG emissions to CDP while considering other platforms that allow for greater flexibility in the approach.

Supporting producers to improve

We are working to help producers, meaning the companies that grow the oil palm tree and harvest the palm fruit, to meet PepsiCo's policies and commitments, including protection of HCV/HCS and peat land, protection of human rights, upholding free prior and informed consent, and encouraging smallholder inclusion. PepsiCo does not source directly from producers or mills, but we believe that providing support through our Palm Oil Action Plan is necessary to drive systemic improvement.

Our producer engagement process starts with our risk assessment and prioritization work. Based on the findings, we are identifying partnership opportunities and developing engagement plans for each of our key sourcing markets, starting with Indonesia and Mexico. In Indonesia, we have identified labor rights, deforestation, peat loss and smallholder inclusion as key issues to address. We are currently talking with a range of stakeholders, including our suppliers and civil society organisations that are actively working on these issues on the ground, to identify potential collaboration. We plan to invest \$250,000 as well as significant time and other resources over the next 12 months in advancing one or more support programs.

In Mexico, where PepsiCo is a relatively major buyer in the palm oil sector, we are endeavoring to take a leading role in bringing together companies, civil society, government and associations to develop and implement a program to support improved practices, including among smallholders.

In other regions from which our palm oil originates, we are currently completing our review process and will develop additional engagement plans by the end of 2017.

VI. Addressing claims of non-conformance with our policies

Key points in this section:

- PepsiCo has developed a grievance mechanism for dealing with environmental and social complaints involving palm oil and other agricultural raw materials in our supply chain.
- We look to engage suppliers and promote corrective actions that help solve problems and build capability for sustainable palm oil. We will consider all appropriate steps if engagement does not lead to progress.
- Consistent with our commitment to the UN Guiding Principles on Business and Human Rights, we have sought to use our relationships to bring resolution to palm oil complaints involving our supply chain, including and beyond our direct suppliers.

PepsiCo has systems in place to proactively address instances of non-conformance with our policies. We aim to identify and address such instances through a combination of risk assessment, engagement and auditing. Due to the complexity of our supply chain, we understand that we cannot be sure to capture every issue. Civil society groups and others play a role in highlighting potential areas of concern regarding producers and suppliers in the palm oil sector, so we speak with them regularly to benefit from their expertise. Given the seriousness of some of the complaints and the complexity of both the supply chains and the issues, PepsiCo has developed a grievance mechanism focused specifically on our palm oil and broader agricultural supply chains (Box 2).

This grievance mechanism is complementary to our existing [Speak Up! Process](#) as well as our Sustainable Sourcing Program, discussed in Section V, which assesses site-level grievances involving workers of direct suppliers. In every case, we look to engage suppliers first and promote corrective actions that solve problems and build capability for sustainable palm oil. In cases where engagement does not lead to progress, we will consider all appropriate steps, including significant action where deemed necessary, as we have done in one recent example that involved removing a supplier from our supply chain.

Our intent is that the Grievance Mechanism will be run on the principles of transparency, consistency, and neutrality. Our experience with grievances raised by third parties until now is that they are often complex, involving multiple actors and differing perspectives on the situation and potential remediation efforts. Our aim is to uphold our policies and to achieve outcomes that help people whose rights may have been affected in a way that is satisfactory to all parties of the complaint.

Among food and beverage companies, we believe our grievance mechanism is leading practice.

Joint ventures (JVs)

As stated in our Palm Oil Action Plan, PepsiCo's palm oil policy and commitments apply to all of its brands and products worldwide. Where direct suppliers are involved, our contracts often provide a basis to verify compliance with our policies, such as the ability to request on-site audits of their mills. With respect to JVs, relationships vary and require specific approaches. For example, in 2015 PepsiCo initiated an ongoing review and engagement effort with Indofood Fritolay Makmur (IFL), our snack food JV in Indonesia. As a result, the JV has moved to 100 percent RSPO certified sustainable palm oil for PepsiCo snack foods.

Considerable attention has been paid to Indofood's broader operations because they include palm oil production, in particular an Indofood subsidiary called IndoAgri Resources. PepsiCo has no contractual relationship with IndoAgri Resources. In April 2016, PepsiCo was informed of labor rights allegations made against IndoAgri Resources by a group of complainants. We take such allegations seriously and are well aware

of environmental and human rights concerns facing the palm oil industry, as reflected in our palm oil policy and commitments.

Box 2: PepsiCo Grievance Mechanism for Our Agricultural Supply Chain

The grievance mechanism for our agricultural supply chain is new and launched as of the publication of this Progress Report. It is open to anyone who has a concern that PepsiCo's policies and commitments related to agricultural commodities and palm oil are not being met. Each complaint goes through the following process:

- Step 1: Receiving the complaint. The complaint is received, logged in the mechanism and acknowledged to the complainant (where appropriate).
- Step 2: Is the complaint in scope? The complaint is reviewed to establish that it is in scope: does it apply to PepsiCo's supply chain and to our policies and commitments? If the complaint is out of scope, it will be closed. If it is in scope, the process will continue to Step 3.
- Step 3: Investigating the complaint:
 - If the complaint is about a direct supplier, PepsiCo will lead the investigation into the grievance, utilizing expertise from our Sustainable Sourcing Program.
 - If the complaint is about a supplier that does not directly supply PepsiCo, we will use our relationships with our direct suppliers that source from the company to develop the appropriate investigative steps where they are not already being undertaken.
- Step 4: Taking action. If actions or remediation are needed these will be agreed to with the supplier and communicated to the complainant (where appropriate).
- Step 5: Monitoring and implementation. PepsiCo will work with the direct supplier or through them to confirm that the agreed actions and remediation are completed, and the case will then be closed.

An internal PepsiCo resource will oversee the process, and a grievance working group including representatives from our procurement, human rights, sustainable agriculture and public policy teams will advise regarding any substantive decisions during the process, including actions to be taken if suppliers refuse to engage with the issues raised in the complaint or do not complete the agreed steps. A Grievance Committee, comprising senior management from the departments represented at the working group level will meet quarterly to review individual cases and the operation of the grievance mechanism, including the implementation of our policies.

Further details of our [grievance mechanism](#) can be found on PepsiCo.com.

Consistent with our commitment to the UN Guiding Principles on Business and Human Rights, we have sought to use our relationships to bring about an appropriate resolution. One of our first actions was a letter to Indofood, the parent company with which we have a JV. The letter came from PepsiCo's Chairman and CEO conveying our concerns and expressing our expectation that Indofood is taking such allegations as seriously as PepsiCo does. Over the past year we have had at least five meetings and calls with the company to discuss the allegations and their actions to address them. For example, Indofood provided a copy of their January 2017 audit report indicating steps in a variety of areas. In addition to working with Indofood, we have also had a similar series of meetings and calls with the complainants to better understand their view of the complaint and solutions to sustainable palm oil.

We also wrote to RSPO, where a complaint was formally filed with respect to IndoAgri Resources' operations. We offered our support to RSPO and encouraged them to continue to execute their complaints resolution

process to arrive at more timely outcomes. This process may involve one or more meetings among the parties to the complaint. PepsiCo has supported a meeting among the parties, and IndoAgri Resources has expressed a willingness to participate. Although the RSPO has offered to facilitate meetings for approximately six months, none have yet occurred. We will continue to encourage the parties to come together to discuss these important issues.

Since beginning this work, IndoAgri Resources has further developed its policy commitments and program on palm oil. We are committed to continuing this engagement to address any outstanding issues and encourage the complainants to leverage the RSPO complaints resolution process to work to an amicable resolution.

VII. Transparency and stakeholder engagement

Key points in this section:

- We have improved our palm oil reporting and expanded our stakeholder engagement to include broader, sustained interaction with civil society organizations and industry platforms.

Our Performance with Purpose agenda includes a sustainability reporting effort across a wide array of topics, including publication of significant volumes of data. As part of our commitment to transparency, PepsiCo provides regular, detailed information to a wide range of interested stakeholders on our Palm Oil Action Plan and progress on delivering on our palm oil commitments.

This Palm Oil Action Plan Progress Report for 2016 is our second report. We have gained a significant amount of experience and learning over the two years since our Action Plan was published, and this report improves upon our format to better illustrate the purpose of our work and how the threads of our Action Plan relate to one another. With this report we are also shifting to an annual, calendar-year reporting cycle, which will be synchronized with our Annual Communication on Progress to the RSPO, meaning we will seek to publish this report in the future in the May/June timeframe. We will also provide periodic interim updates on our web site as appropriate.

Our palm oil work does not exist in a vacuum, and as we have stated throughout this report, we believe partnership and collaboration are vital. We have frequent, proactive engagement with many stakeholders on all of the key palm oil issues identified in our Action Plan. We learn from these stakeholders, gain a more rounded understanding of the opportunities and challenges in the palm oil sector, and contribute wherever we can. We are open to engaging with any organization that is willing to work constructively with us.

The following are some examples of our engagement efforts over the past year:

- **NGO community:** PepsiCo had numerous meetings and conversations with NGOs that work on palm oil, including Greenpeace, Oxfam, RAN, WWF and others. For example, we participated in Oxfam's palm oil workshop at the annual RSPO Roundtable where the importance of pre-competitive collaboration among all actors, including civil society, was highlighted.
- **RSPO:** PepsiCo was a sponsor of the RSPO Annual Conference in Bangkok, and we organised a knowledge sharing webinar with our procurement team and RSPO on how best to transition to the new RSPO Credits and implement Chain of Custody Certification. We are in regular contact with their regional staff.
- **Consumer Goods Forum:** We participate in the CGF's Palm Oil Working Group and, as noted above, helped lead two industry webinars on mill traceability, which we hope will promote interoperability of data systems and the acceleration of traceability across the industry.

- **AIM-Progress:** PepsiCo is an active member of the AIM-Progress leadership team and co-chaired the human rights work stream in 2016. AIM-Progress focuses on improving sustainability within supply chains, and we co-sponsored a supplier engagement in Bangkok, Thailand in October 2016 focused on forced and migrant labor, overtime hours, grievance mechanisms and discrimination.
- **IDH:** PepsiCo actively participates in the Landscapes Working Group coordinated by the IDH Sustainable Trade Initiative. One of the goals is to define traceability to the farm/plantation level. This will be developed with input from a wide range of companies and other stakeholders to align on an industry definition for traceability to plantation.
- **Tropical Forest Alliance (TFA) 2020 membership:** PepsiCo attended the annual General Assembly and Partners Meeting in Brasilia and subsequently joined the organization as a member. TFA 2020 is a global public-private partnership in which partners take voluntary actions, individually and in combination, to reduce the tropical deforestation associated with the sourcing of commodities such as palm oil, soy, beef, and paper and pulp.

Through our extensive engagement, we have heard specific points of criticism about the need to move farther and faster. We are, however, encouraged by acknowledgement of our progress. In 2016, for example, our Action Plan was evaluated by the World Wildlife Fund in a global ranking of consumer goods companies. PepsiCo received the highest possible score from WWF for leading the way on progress on essential actions on sustainable palm oil. Our scorecard can be viewed on WWF's web site: <http://palmoilscorecard.panda.org/check-the-scores/manufacturers/pepsico>.

Next steps

PepsiCo's Palm Oil Action Plan is a multi-year program designed to enable our company to play its part in the long-term transformation of the palm oil industry. We take this work seriously, and our palm oil team was able to initiate and complete substantial threads of work in 2016 that set the stage for further progress in 2017 and beyond. As we publish this 2016 Progress Report, we note the following priority items currently in our pipeline of work, and we look forward to sharing progress on these and other items in future reports:

- **Mill traceability:** We are implementing our approach to third-party verification of the data reported to us by our direct suppliers. We will continue the quarterly reporting cadence from suppliers with a view to 100 percent traceability to the mills.
- **Physical certification:** We continue to execute against our global roadmap to purchase 100 percent physically certified RSPO sustainable palm oil by 2020, and we are targeting 30 percent of our volume by the end of 2017. In many cases, this includes developing supplier capabilities as well as investing in new supply chains.
- **Direct supplier engagement:** We continue to develop our program, including risk-based prioritization of engagement and roll out of our new supplier scorecard.
- **Impact Programs:** PepsiCo will bring new investment to one or more impact programs in Southeast Asia, including Indonesia, utilizing input and collaboration with a variety of stakeholders, including suppliers and civil society organizations.
- **Grievance mechanism:** We are implementing our new grievance mechanism related to palm oil production and our broader agricultural supply chain.

Appendix: PepsiCo's Palm Oil Action Plan Commitments, October 2015

- Source 100% certified sustainable palm oil (CSPO) by 2015.
- Ensure all direct suppliers are RSPO Members by 2016.
- Engage with appropriate industry and other groups to improve our understanding of concerns within the palm oil industry and to achieve our goals.
- Map supply chains to the mill of origin to ensure traceability by 2016.
- Implement a third-party audit program for Forestry Stewardship and Land Rights policies for our palm oil supply chain.
- Actively assess risk of our global palm oil suppliers and source countries and engage with those suppliers operating in high-risk regions to carry out on-the-ground assessments of practices.
- Request our palm oil suppliers to report on greenhouse gas emissions through the CDP Supply Chain, or similar program.
- Suppliers, as necessary, will be encouraged to adopt high standards for palm oil sustainability throughout their systems.
- Ask suppliers to identify the use of derivatives in our ingredients.
- Work with suppliers to ensure that PepsiCo's palm oil policies are implemented in a way that supports the inclusion of smallholders.
- Leverage the PepsiCo Sustainable Farming Initiative to support implementation of sustainable agriculture practices that enable farmers to increase production on currently farmed land and minimize impacts on the surrounding area.
- Ensure PepsiCo's palm oil supply chain understands PepsiCo's expectations under our Supplier Code of Conduct.
- Ensure that PepsiCo's palm oil sources will be in compliance with PepsiCo's Forestry Stewardship Policy, which includes adherence to principles regarding High Carbon Stock (HCS) Forests, High Conservation Value (HCV) areas, and no new development of peat lands.
- Ensure that PepsiCo's palm oil sources will be in compliance with PepsiCo's Land Use Policy, which includes adherence to the principle of Free Prior and Informed Consent (FPIC).
- PepsiCo will apply its policy and commitments to all its brands and products worldwide.
- Map supply chains from mills to farm/plantation level by the end of 2020.
- Source 100% physically certified sustainable palm oil by 2020.
- Periodically report on our progress against our policies, commitments, and this action plan.