

## Supply Chain Responsibility

### Objectives and points of departure of this memorandum

With this document, the participants in the MVO Platform are laying down their joint vision regarding the subject of supply chain responsibility. The objective of this document is:

- to identify the responsibilities of civil society organisations, in order to make their expectations in this area clear;
- to make a contribution to the coherence of the debate about supply chain responsibility;
- to supplement the advice *Sustainable Globalisation, a world to be won* which the government received this summer from the Socio-Economic Council (SER);
- to make recommendations to the government and the business community.

This joint vision is based on the international system of rights, obligations, standards and guidelines applicable to CSR, as described in the *CSR Frame of Reference*.

That a company bears responsibility for its production and trade chains is determined in the definition of corporate social responsibility (CSR) applied by the MVO Platform in its CSR Frame of Reference: *“CSR is a process whereby a company assumes responsibility, across its entire supply chain, for the social, ecological and economic consequences of the company’s activities, reports on these consequences, and constructively engages with stakeholders.”*

The point of departure is therefore a responsibility for the entire supply chain. The extent to which a company is responsible within a chain is determined, among other things, by the influence of the company and the seriousness of possible abuses.

The text below describes the voluntary supply chain responsibility which is being worked towards for companies in 2008 and the current role played by the public sector and civil society organisations. It also addresses supply chain transparency and supply chain liability.

The MVO Platform considers greater supply chain transparency (openness of companies) to be of great importance to taking the existing voluntary supply chain responsibility to a higher level. Supply chain liability (the legal anchoring of supply chain responsibility) makes it possible for minimum requirements to apply to all businesses.

### 1. Introduction: who monitors the internationally operating enterprises?

In the area of human rights, employment conditions and the environment, companies are regularly involved in abuses in their trade and production chains (hereinafter referred to as: chains). There are particular problems in developing countries, where companies which operate on the Dutch market have a great many trade contacts.

Abuses can occur in all links in chains. They sometimes occur at the start of the chain (for example, environmental contamination resulting from oil mining or other mining activities, and child labour in cotton cultivation), sometimes they occur halfway along the chain (such as labour conditions in sweatshops), sometimes in the usage phase (for example in the weapons industry) and sometimes in the waste phase (for example, dumping electronics and dismantling ships). In all these cases, and in various ownership and trade relationships, supply chain responsibility exists according to the MVO Platform.

For various reasons, governments only want to direct and assess the internationally operating business community to a limited extent. International standards for human rights, labour conditions (ILO) and the environment are difficult to enforce in law. Even if companies break the law, the legal options are limited.

International standards which apply to businesses inside their sphere of influence only exist for the most fundamental human rights. Inasmuch as these standards are anchored in Dutch legislation (including criminal legislation), there is the *International Crimes Act*. This includes complicity in war

crimes. Even if breaches take place outside the Netherlands, the company established in the Netherlands is criminally liable. Other enforceable international standards are against corruption, for example, and for liability in the case of certain disasters, such as an oil disaster. This summarises all international standards which can be legally enforced.

Special Representative of the UN Secretary-General on business & human rights, John Ruggie, concluded in April 2008 that governments have insufficient administrative options available to them to combat negative human right consequences of the globalised marketplace. Ruggie refers to these as *governance gaps*. Professor and European expert in the area of liability law Cees van Dam summarised this in his recent publication *Onderneming en mensenrechten* ('Enterprise and human rights') as follows: 'Trade has been globalised, justice not yet.'

A number of multinationals are taking active responsibility for the observance of human rights, employment conditions and preservation of the environment within their supply chains. They impose codes of conduct on their suppliers and have control systems for monitoring compliance. These agreements between clients and suppliers come into being on a voluntary basis. It is not obvious in this context that internationally accepted standards form the basis. But it is an important start.

The current voluntary practices - defined according to the insights of each individual company - in the area of supply chain responsibility are, however, contributing insufficiently to:

- a good living environment for people;
- sustainable development, human rights and labour rights;
- protection of consumers against unsustainably produced products;
- animal welfare.

Finally: due to the continuing globalisation, the business community is gaining greater influence. Companies can play a real role in compliance with and strengthening of international standards in the area of human rights, employment conditions and the environment. Up to now, governments have created insufficient opportunities for assessing and directing the business community. Consumers, trade unions, civil society organisations and several companies are therefore calling on governments to place an obligatory base in the market by means of minimum requirements, and to support voluntary improvements above this.

## 2. Supply chain responsibility: a three-stage rocket

In the debate about supply chain responsibility, the MVO Platform considers three positions to be important.

Firstly, **supply chain transparency and traceability** are relevant. In order to flesh out supply chain responsibility – including the version being promoted by the Dutch government – it is necessary that companies are more open about the origin of their products and about how they deal with social problems occurring in their supply chains (their supply chain management).

Secondly, it is important to promote **voluntary supply chain responsibility**, which companies are currently taking on voluntarily and on the basis of self-regulation, in order to make chains more sustainable. Governments and civil society organisations can stimulate companies in this respect in a large number of ways.

Thirdly, it is necessary to **legally anchor** minimum requirements for supply chain responsibility in order to be able to tackle abuses and free riders (supply chain liability).

### 3. Supply chain transparency

Companies can be more transparent about the chains in which they operate and the role they fulfil in them in a variety of ways:

- statements in the annual sustainability report of what the social and environmental circumstances are under which products and services come into being in their chains;
- indicating which codes of conduct and control systems, including international standards relating to corporate social responsibility, are applied, and describing the implementation thereof;
- participation in a certification (process), so that the consumer obtains information on the nature and extent of a product's sustainability. Examples include the FSC label for wood, the MSC label for fish, the Fairtrade mark and the EKO mark;
- providing accountability - proactively - on social problems with which the company is closely involved (such as climate change or alcohol use among young people). Furthermore, the company can indicate how it contributes to tackling the problem;
- providing information, on request, to consumers, corporate customers and civil society organisations. For example, consumers ask about the way in which products are made, so that they can take this information into account in their choice of product. Civil society organisations request information which is only available at the company, in order to be able to contribute to improvements in the company's supply chains.

In 2008, the Dutch government uses various instruments to promote traceability of products and supply chain transparency by companies. The most important are:

- food safety legislation;
- the annual Transparency Benchmark on CSR reports of the 200 biggest Dutch companies;
- The objective of the Dutch government to only purchase sustainably as of 2010;
- information to consumers (limited for the time being) about certification ([www.consuwijzer.nl](http://www.consuwijzer.nl));
- the possibility to tackle misleading hallmarks on end products via the Consumer Authority.

The government does not yet have any requirements for free riders. It can take a number of additional measures on supply chain transparency. The legal anchoring of supply chain responsibility (supply chain liability) must be regulated in the context of the European Union. But companies and the Dutch government can take initial steps in supply chain transparency themselves. The government can make it obligatory to draw up annual sustainability reports, including criteria with which the reports must comply (for example guidelines of the Global Reporting Initiative or the Foundation for Annual Reporting) and impose sanctions in the event of non-compliance.

The government can also give the consumer the right to information on certain ethical aspects of the production process. In this way, compliance with CSR standards is elevated to a quality of a product, and consumers are given the opportunity to accept their role as aware players in the market, and to vote with their wallets. Competition between the various producers, driven by aware consumers, will lead to an improvement in compliance with these standards by internationally operating companies. Finally, the Dutch government can oversee this and encourage companies to involve their stakeholders more structurally in their supply chains, in their home countries but also in the country which problems are occurring.

### 4. Voluntary supply chain responsibility

It raises hope that supply chain responsibility is becoming an acknowledged important CSR aspect. Governments and companies are no longer flatly denying their responsibilities. Pioneering companies are taking steps to improve production conditions.

### **The relevance of the business community**

Supply chain responsibility is important for companies in order to lower the risk of value destruction (loss of reputation) and/or to realise value creation (creating an image in the marketplace). It is the responsibility of businesses to create sustainable value for all stakeholders. This value consists, among other things, of good business operations, good employment conditions for employees/suppliers, and a healthy living environment and return for the shareholders.

Supply chain responsibility implies clarity and dialogue with stakeholders about the sustainability requirements set of suppliers. In a broader context, the applicable CSR requirements are incorporated in codes of conduct and objectively laid down in verifiable standards with clear control systems for monitoring compliance. Above all, supply chain responsibility is integrated in purchasing policy, product development, control of the production process and chain and the risk management systems connected to them. Various companies are already doing this, in a fragmented form.

Good control of the product and production process throughout the entire chain can result in satisfied employees who remain employed for longer, and in greater trust by customers and business partners. It also contributes to sustainable development. A partial or fragmented responsibility can result in legal and financial consequences and damage to the reputation of a business or product.

### **The role of civil society organisations**

Civil society organisations can play an important role if they enter into a constructive dialogue in the long term with a company or with an entire sector (via a sector or multi-stakeholder initiative), propose solutions for abuses and demonstrate the added value of supply chain responsibility. This can be in their home country, but also in particular in the country in which problems are occurring. Civil society organisations have a function as countervailing power against the established powers of government and the business community. They are the 'social conscience'.

Civil society organisations expose abuses and unwillingness to improve on the part of companies, sometimes by public opinion. Companies who are sensitive to damage to their reputations, for example because they are clearly dependent on (and visible to) certain stakeholders such as consumers, can be influenced by means of such a negative approach. The positive aspect of this approach is that public opinion becomes aware of abuses, and therefore gives greater support to the need for regulations by the government.

Civil society organisations can use laws already in existence to boost the legal possibilities for supply chain responsibility through case law. Up to now, the existing law has barely been tested.

In the event of abuses, civil society organisations can also submit a complaint against a company which in their opinion is not complying with the OECD guidelines. The National Contact Point (NCP) in the Netherlands no longer restricts itself to investment-related subjects, for example, but also claims to incorporate abuses in supply chains.

### **Government measures**

The Dutch government promotes supply chain responsibility among businesses, particularly if they have entered into a direct relationship with the government. Examples include:

- CSR assessment in the case of financing and credit insurance, such as is already taking place via the foreign financial toolkit;
- Setting CSR conditions for subsidy schemes (for example, setting sustainability criteria for biomass);
- CSR assessment during trade missions.

The government can reach a great many companies through this dependent relationship.

Evaluating companies on the CSR quality of their activities can include more, however, such as compliance with the OECD guidelines for multinational enterprises, supplemented by concrete requirements in the area of social aspects, environmental policy and corruption (bribery). An important initiative in the Netherlands relating to child labour in the supply chains of companies is the motion by House member Voordewind, which was adopted by the entire House. This argues that companies which receive government support (for example subsidies, credits or participation in trade missions) must make it transparent that they do not use any child labour in their supply chains. If companies do not do this, they must have a 'public, time-limited plan' to get children to school, otherwise the government support is stopped. Work is currently taking place to convert the motion into concrete plans. The same principles which are in the motion - transparency and visible action to tackle abuses - should also be applied to other (fundamental) labour standards and environmental standards.

The Dutch government can use the policy to only purchase sustainably as of 1 January 2010 to give a significant impulse to sustainable production/consumption and stimulate a great many more companies to take responsibility for their chains. Not only the government commissions themselves, but also the fact that as a result a company receives recognition for its sustainability, increase the market opportunities for suppliers of sustainable products and services.

The government's objective is that purchases and tendering of the State government will be 100% sustainable in 2010. The municipalities want to have 75% sustainable purchases in 2010, and provinces and water boards, 50%. The policy must be fleshed out in more concrete terms. Because it may be the case that politicians decide which social criteria are applied (in particular, the fundamental labour standards), but it is not yet decided how these are then used. For example, how far in the supply chain the responsibility reaches and how the verification will take place. In addition, the environmental criteria are fairly weak and, as with the social criteria, have not been applied to the majority of the product groups.

The government must make haste in order to achieve its objectives in 2010. A major part of the delay lies in the question of what is legally permitted, in which matter various schools of legal thought are in disagreement. EU legislation is vague, but this rather leaves room for experimentation - the Swedes are already using a wide range of social criteria in their tendering and have laid down sustainable purchasing in law. The unclear EU legislation provides an impetus to obtain greater clarity from the European Union, or otherwise to create a clear Dutch legal framework for it ourselves.

The Dutch government, together with various stakeholders, set up the Sustainable Trade Initiative (IDH) in 2008. The IDH is intended to make several products and services used in the Netherlands more socially responsible and to focus on the start of the chain in this respect. The IDH focuses on initiatives of specific companies and stakeholders. For the time being, these are the soya, tropical wood, cocoa, natural stone, tea and tourism sectors.

## **5. Legal anchoring of supply chain responsibility: supply chain liability**

Companies which are involved in abuses in the chains from which they source their products or in which they offer their services have, up to now, not been punishable by law, or only to a very limited extent. They can decide themselves whether to take action against breaches of standards or laws in their supply chains. Rules on supply chain liability can put an end to this undesirable situation.

Supply chain traceability and liability are already accepted phenomena in the food sector. Food safety is the major social issue in this respect. Food companies in Europe are obliged to document the origin and destination of ingredients used in the chain, in such a way that they can deliver the requested information to the authorities within two working days. This traceability requirement has been laid down in the European General Food Law since 2005, based on the preventive ISO 22000 (HACCP) standard. Furthermore, under the Product Liability Act, in the event of breaches of food and product safety rules, the Food and Consumer Product Safety Authority holds the retailer liable and not the

supplier. This supply chain traceability and liability for food safety is easy to combine with corporate social responsibility. The example shows that the business community is able to monitor its supply chain if social problems occur can occur which arouse interest.

For a limited number of sectors and abuses, the European Union is already working on supply chain liability which goes beyond more tightly defined product safety requirements. For example, the EU wants to combat the trade in illegally felled timber through the FLEGT action plan (*Forest Law Enforcement, Governance and Trade*). This will require timber traders to monitor their chains. Another initiative to be encouraged is the investigation which the EU will be carrying out into the possibilities for an import ban on products realised with the worst forms of child labour. In addition to a possible import ban, measures are also needed to help the children involved to transition from work to school and to help the adults find 'decent' work inside or outside the sector.

In addition to illegal felling and child labour, there are other CSR abuses in chains. It is highly likely that rules will be introduced in this context. It must be possible to take legal action against companies in their homelands if they are involved in maintaining illegal and/or unacceptable practices in their chains.

The legal touchstone for the determination of whether a company is guilty or not can be the answer to the following question: can the court in all reasonableness convict a company for maintaining the abuses? In a concrete case, questions are addressed such as: could the company have known about the abuses in its supply chain?; how serious are the abuses?; which steps has the company taken to prevent abuses, to work on improvements, to stop the involvement in the abuses?; to which extent do the abuses take place within the sphere of influence of the company?

The European Coalition for Corporate Justice ([www.corporatejustice.org](http://www.corporatejustice.org), a platform for EU country organisations, including the Dutch MVO Platform) is arguing at the EU for regulations governing supply chain liability on such a basis. The argument is in line with the Global Reporting Initiative and a study by the Danish Institute for Human Rights. The GRI Boundaries Protocol of the Global Reporting Initiative makes the action perspective and the responsibility for it dependent on the level of influence and the nature of the impact. In its report *Complicity in human rights violations: a responsible business approach to suppliers*, the Danish Institute for Human Rights applies for basic principles to determine the extent of responsibility. These are: the level of dependence of the supplier on the client (enabling principle), the causality principle, the seriousness of the breaches and the level of influence.

If legislation is introduced for liability in the home countries (including sanctions), companies will have to make greater efforts to reduce their involvement in abuses. Legislation on its own will therefore have a preventive effect and reduce the number of abuses. By ensuring that not only European companies but also companies which are active on the European market fall under the legislation, a global level playing field for companies is within reach.

However, more is needed before the legislation will have social dynamics and case law. We identify two important conditions below. In the first place, access to justice for plaintiffs outside Europe must be improved, both legally and financially. Secondly, it must be possible to force companies to provide access to information. This is because it is often only possible to get answers to the above legal questions from the company itself.

## **6. Supply chain responsibility and small producers**

There is a downside to increasing quality and sustainability requirements: global inconsistency and confusion. This can be a disadvantage primarily to small producers who do not have the manpower or resources to be able to comply with all the requirements. One example of an apparent negative effect is GlobalGAP, one of the few certification systems which require strict compliance with minimum

requirements and exclude consistent producers who do not comply with these, including many small farmers.

From the point of view of manageability and clarity, there is a visible trend among businesses of a 'concentration of suppliers' (with the supplier often larger than the brand). This can be seen as a positive step backwards in globalisation (no longer buying everywhere, an end to the 'race to the bottom'). However, this monopolisation also leads to a major concentration of strength and global dependence on a small number of large companies, to a loss of diversity and to an increasing exclusion of smaller producers and producer groups and, on balance, to a loss of jobs.

One answer to these problems for the small producers is for the Global Standard Setting Bodies which develop the standards and sustainability requirements to build in measures to strengthen the capacities of chain partners so that they can demonstrably comply and continue to comply with the requirements in the chain. Civil society organisations can also play an important role in this.

A comparable insight which occurs in practice (for example, with purchasers who are united in the Ethical Trading Initiative) is the incompatibility between compliance with CSR requirements on the one hand and purchasing practice which demands ever lower prices and ever greater flexibility from suppliers, on the other. Only if all companies within a certain (global) production chain implement and facilitate codes of conduct both in production and in purchasing can a facilitating environment and a level playing field be created. The Tropical Commodity Coalition (TCC) is working to realise this objective for coffee, tea and cocoa. This objective is also being worked on in other chains.

### **Recommendations for the Dutch government**

The above analysis leads to the following recommendations of the MVO Platform to the Dutch government:

1. **Supply chain liability.** It must be possible to take legal action against companies in their homelands if they are involved in maintaining illegal and/or unacceptable practices in their supply chains. The Dutch government must work to achieve regulations on supply chain liability, in the Netherlands and in the EU. In order to ensure greater strength and to work towards a level playing field for all companies, EU regulations for companies which are active on the European market are preferable to Dutch regulations. In areas in which the EU does not yet have any policy, the Netherlands can take the first step by developing its own regulations. Improving access to law and information is necessary in order to make the regulations effective.
2. **Supply chain transparency.** The Dutch government must make traceability and transparency on the part of companies at the production process level and the product level mandatory. Consumers have a right to know under which circumstances products or services come into being, so that they can take their own responsibility for sustainable consumption. Civil society organisations need this information in order to be able to contribute to improvements in the supply chains of companies.
3. **Sustainable purchasing by the government.** Sustainable purchasing must be given a legal basis, as is already the case in Sweden, among other places. Supply chain responsibility must form a part of this. The current objective, for all purchasing and tendering out by the State government to be 100% sustainable by 2010 (100% should also apply to municipalities, provinces and water boards), will only be achieved once the frequent breaches of rights and environmental damage taking place in supply chains are also actually tackled.
4. **Other recommendations to the government:**
  - a. supporting the countervailing power in society (for example trade unions, non-governmental organisations and other civil society organisations), so that they can contribute to making society sustainable;

- b. contribution to and investment in a facilitating environment in producer countries, both at the level of the national government and at the level of producers, so that they have the capacity to comply with CSR requirements in the supply chain;
- c. integration in the trade policy of the international obligations arising from international law, and making them a permanent part of trade negotiations and agreements, also in an EU context;
- d. working to achieve coherence between the various government agencies in the area of sustainability and CSR;
- e. monitoring and evaluating the actual effects of CSR policy on people and the environment, including progress in the area of sustainable purchasing.
- f. corrective action, for example by withholding government support in the event of a breach of OECD guidelines and other breaches of international standards.
- g. stimulating and supporting efforts made by companies to improve their CSR behaviour in the supply chain and by actually implementing the recommendations below.

**Recommendations to the business community in the Netherlands:**

- a. ensure transparency throughout the supply chain and work in a targeted manner and to a timetable on improving sustainability standards in the chain;
- b. determine which CSR problems need the most attention in the trade and production chain ('know your chain') and take active steps to prevent, reduce or end problems by applying influence on suppliers (vertical approach);
- c. as much as possible, choose suppliers who can demonstrate that they comply with sustainability standards and suppliers who offer preconditions for compliance with CSR requirements;
- d. the creation of a level playing field and increasing collective influence on other members of the sector in a specific chain (horizontal approach), particularly where a company is not independently able to realise improvements (for example, by taking chain initiatives);
- e. striving to be one of the best in the area of CSR in the sector or chain in question, and to be a good example to others;
- f. actively involving local involved parties/stakeholders (civil society organisations, trade unions, employers' organisations, the government) in the country in which the problems are occurring and in the company's home country, in obtaining insight into and solving problems, and meeting social expectations. It is crucial in this respect that accountability is rendered to these groups in the area of supply chain responsibility.