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Global sourcing through foreign subsidiaries and suppliers: Challenges for Corporate Social Responsibility

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Introduction

Most transnational corporations increasingly rely on foreign subsidiaries and suppliers for their production of goods.¹ Companies have usually developed a sophisticated and complex global sourcing strategy in order to reduce costs.² Following recurrent reports about human rights violations at supplier factories in the developing world, many companies pursue a sustainable supply chain management policy.³ They publicise information about how they work towards improving working conditions in their corporate group and supply chain. This engagement is usually part of the companies' Corporate Social Responsibility (CSR) agenda.

However, from a legal perspective, the use of foreign subsidiaries and suppliers constitute significant challenges for the promotion of CSR.⁴ The territorial nature of law, the separate legal personality of companies and weak law enforcement mechanisms in the developing countries where the production takes place create loopholes which make it difficult to hold Western transnational corporations legally accountable for irresponsible corporate conduct within their global production network.⁵ This chapter will first look at the challenges for CSR posed by the use of foreign subsidiaries and suppliers in their global sourcing. It will then critically discuss to what extent the home state of transnational corporations could fill those gaps by legal regulation.⁶ To that end, the chapter will discuss tort law, criminal law and disclosure requirements. It will also critically review if the multi-stakeholder initiative Accord on Fire and Building Safety in Bangladesh, created after the Rana Plaza building collapse, could be a model for the future promotion of CSR.⁷ The chapter will argue that it is time that the home states of transnational corporations accept their responsibility for regulating the

¹ See L Mosley, *Labor Rights and Multinational Production* (CUP 2011) 17.

² A Millington, 'Responsibility in the Supply Chain' in A Crane, A McWilliams, D Matten et al. (eds), *The Oxford Handbook of Corporate Social Responsibility* (OUP 2008) 363.

³ R Monczka et al., *Purchasing & Supply Chain Management* (4th edn, South Western 2010) 377.

⁴ A Rühmkorf, *Corporate Social Responsibility, Private Law and Global Supply Chains* (Edward Elgar 2015) 213-233.

⁵ A Rühmkorf, Global supply chains: the role of law? A role for law! *OpenDemocracy* (2 March 2015), available at <https://www.opendemocracy.net/beyondslavery/andreas-r%C3%BChmkorf/global-supply-chains-role-of-law-role-for-law> (accessed 22 June 2015).

⁶ The term 'home state' is used in this chapter to refer to the state in which the transnational corporation is incorporated and where it has its administrative centre. The host state is the state in which the transnational corporation operates, either directly or through its subsidiary. See B Cragg, 'Home is where the halt is: Mandating Corporate Social Responsibility through home state regulation and social disclosure' (2010) 24 *Emory International Law Review* 735, 751.

⁷ Accord on Fire and Building Safety in Bangladesh, available at <http://bangladeshaccord.org> (accessed 20 June 2015).

socially responsible conduct of those companies. In terms of its jurisdictional scope, the chapter focusses on English law.

1. Global sourcing strategies: The use of foreign subsidiaries and suppliers

The outsourcing of the production of goods is an important strategic tool of transnational corporations to remain competitive.⁸ This is particularly the case in cost-driven industries such as the garment industry or in the production of electronic devices.⁹ Whilst in these instances companies try to reduce the cost of manual labour, other industries such as the confectionery industry need the supply of raw materials from overseas, for example cocoa beans.¹⁰ The global sourcing strategy of many transnational corporations includes foreign subsidiaries and/or suppliers, often based in the developing world.

Whilst companies have always sourced raw materials from overseas, the strategic use of manual labour as a cost-saving tool has particularly developed since the early 1990s.¹¹ Transnational corporations employ different global sourcing strategies: They can use directly-owned foreign subsidiaries for the production or local firms as contractual partners (suppliers).¹² Where trade takes place between transnational corporations and their subsidiaries abroad, and between foreign subsidiaries in different countries, this is referred to as 'intrafirm sourcing'.¹³ Over the last decades, many transnational corporations have developed their global production mechanisms in a way that they increasingly use suppliers instead of wholly-owned subsidiaries.¹⁴ Under this sourcing strategy, the production relies on independent foreign suppliers.¹⁵ These suppliers are linked to the transnational corporation through contracts and together they form a network of suppliers.¹⁶

⁸ S Chopra and P Meindl, *Supply Chain Management: Strategy, Planning, and Operation* (5th edn, Pearson 2013) 155.

⁹ I Mamic, 'Managing Global Supply Chain: The Sports Footwear, Apparel and Retail Sectors' (2005) 59 *Journal of Business Ethics* 81.

¹⁰ D Goodyear, 'The future of chocolate: why cocoa production is at risk' (The Guardian, Sustainable Business - Fairtrade partner zone) available at <http://www.theguardian.com/sustainable-business/fairtrade-partner-zone/chocolate-cocoa-production-risk> (accessed 20 June 2015).

¹¹ R Monczka et al., *Purchasing & Supply Chain Management* (4th edn, South Western 2010) 191.

¹² L Mosley, *Labor Rights and Multinational Production* (CUP 2011) 19.

¹³ M Kotabe and J Murray, 'Global sourcing strategy and sustainable competitive advantage' (2004) 33 *Industrial Marketing Management* 7, 9.

¹⁴ See M Andersen and T Skjoett-Larsen, 'Corporate social responsibility in global supply chains' (2009) 14 *Supply Chain Management: An International Journal* 75, 77.

¹⁵ M Kotabe and J Murray, 'Global sourcing strategy and sustainable competitive advantage' (2004) 33 *Industrial Marketing Management* 7, 10.

¹⁶ S Cavusgil, G Knight and J Riesenberger, *International Business: The new realities* (3rd edn, Pearson 2014) 474.

The organisation of the supply chain, which commonly spans over different continents, is described as supply chain management.¹⁷ The supply chain can be developed in a way that the whole production process is outsourced and transnational corporations purely organise the production process and retain the brand. A good example is NIKE that has, for decades, designed and marketed shoes in the United States which are all produced in factories abroad where the production costs are lower.¹⁸ This strategic separation of the company's headquarter in the global North and West and the factories in the developing world has now become a standard business strategy, particularly in cost-driven industries such as the textile industry.

However, whilst there are clear economic benefits of creating a complex global supply chain, there are recurrent reports about human rights violations such as the use of forced labour at foreign factories. Such incidents have had a negative impact on the reputation of Western transnational corporations that source from suppliers in the developing world.¹⁹ As a consequence of increasing public and political pressure, many transnational corporations have developed sustainable supply chain management as a strategic instrument to demonstrate that they are socially responsible in their global sourcing process.²⁰ Companies with a global supply chain now commonly have CSR policies in place that address issues such as the prohibition of forced labour. To that end, many Western transnational companies have developed their own CSR code of conduct or have signed up to an international CSR standard.²¹ The company's own foreign subsidiaries often adopt the same or a similar code of conduct. As the suppliers are not owned by the transnational corporation, the Western companies as the buyers in the supply chain regularly use their bargaining power to incorporate their CSR code of conduct into their supply chain contracts.²²

Whilst it is evident that transnational corporations have increasingly addressed CSR issues in their global supply chain, the effectiveness of these regimes is a different question. Despite at least two decades of CSR policies, the reports about CSR violations repeat themselves.²³ The 2013 Rana Plaza

¹⁷ See for an introduction S Chopra and P Meindl, *Supply Chain Management: Strategy, Planning, and Operation* (5th edn, Pearson 2013).

¹⁸ See for a description of NIKE and the athletic footwear industry: R Locke, *The Promise and Limits of Private Power: Promoting Labour Standards in a Global Economy* (CUP 2013) 47-51.

¹⁹ R Locke et al., 'Beyond corporate codes of conduct: Work organization and labour standards at NIKE's suppliers' (2007) 146 *International Labour Review* 21.

²⁰ See M Andersen and T Skjoett-Larsen, 'Corporate social responsibility in global supply chains' (2009) 14 *Supply Chain Management: An International Journal* 75.

²¹ D Wells, 'Too Weak for the Job: Corporate Codes of Conduct, Non-Governmental Organisations and the Regulation of International Labour Standards' (2007) 7 *Global Social Policy* 51, 52.

²² E Pedersen and M Andersen, 'Safeguarding corporate social responsibility (CSR) in global supply chains: how codes of conduct are managed in buyer-supplier relationships' (2006) 6 *Journal of Public Affairs* 228, 237.

²³ See for example: The Guardian, 'Sweatshops are still supplying high street brands' (28 April 2011), available at <http://www.theguardian.com/global-development/poverty-matters/2011/apr/28/sweatshops-supplying-high-street-brands> (accessed 30 June 2015).

building collapse is a strong reminder of the fact that we are far off from having achieved responsible corporate conduct throughout global supply chains.²⁴

2. Legal challenges for CSR through foreign subsidiaries and suppliers

This situation raises the question to what extent global sourcing through foreign subsidiaries and suppliers constitute legal challenges for the promotion of CSR.

2.1. No binding international law framework

So far, the legal discussion about CSR and transnational corporations has been particularly prominent in the public international law literature.²⁵ It is important to note that there is no binding international human rights framework for transnational corporations. International human rights initiatives for transnational corporations are primarily soft law. For example, the UN Global Compact which is widely adopted by companies as part of their CSR agenda was not intended to be a 'regulatory instrument'.²⁶ The Global Compact contains ten principles on human rights, labour standards, environmental protection and fighting corruption, but it is not a code of conduct.²⁷ Corporations who have subscribed to it are required to submit examples of how they have complied with the Principles on an annual basis.²⁸ The only control mechanism of the UN Global Compact is that the Global Compact can exclude members who severely violate the principles.²⁹

In recent years, the UN Guiding Principles of Businesses and Human Rights have been the focal point of discussions about the responsibilities of transnational corporations for the working conditions at factories abroad that they source from.³⁰ The Guiding Principles were the result of the six year mandate of Professor John Ruggie as UN Special Representative for Business and Human Rights.³¹ They have been called 'a landmark in the CSR debate'.³² The normative contribution of the Guiding

²⁴ See for a comprehensive coverage of the Rana Plaza disaster <http://www.theguardian.com/world/rana-plaza> (accessed 25 June 2015).

²⁵ See, for example, J Zerk, *Multinationals and Corporate Social Responsibility: Limitations and Opportunities in International Law* (CUP 2006).

²⁶ See UN Global Compact, <http://www.unglobalcompact.org/AboutTheGC/index.html> (accessed 26 June 2015).

²⁷ J Zerk, *Multinationals and Corporate Social Responsibility: Limitations and Opportunities in International Law* (CUP 2006) 259.

²⁸ See UN Global Compact, <http://www.unglobalcompact.org/AboutTheGC/integrity.html> (accessed 26 June 2015).

²⁹ UN Global Compact, Integrity Measures.

³⁰ The UN Guiding Principles refer to the company's value chain in principle 17 'Human Rights Due Diligence', see United Nations, Guiding Principles on Business and Human Rights: Implementing the United Nations "Protect, Respect and Remedy" Framework (New York and Geneva 2011), available at http://www.ohchr.org/documents/publications/GuidingprinciplesBusinesshr_en.pdf (accessed 20 June 2015).

³¹ See the website of the Special Representative of the Secretary-General on human rights and transnational corporations and other business at: <http://business-humanrights.org/> (accessed 28 June 2015).

³² J Ames, 'Taking responsibility' (2011) *European Lawyer* 15.

Principles lies not in the creation of new international law obligations, but in elaborating the implications of existing standards and practices for states and businesses.³³ The Guiding Principles distinguish between the duties of states and the responsibilities of companies in order to indicate that respecting rights is not an obligation that current international human rights law generally imposes directly upon companies.³⁴ The Guiding Principles are intended to be implemented by countries and by companies.³⁵ This aspect is important as it recognises that there is a role for the home state of transnational corporations to regulate transnational corporations.

2.2. The limiting effects of the shareholder value theory for the promotion of CSR

Transnational corporations in the United Kingdom or the United States operate within the shareholder value paradigm which is based on an agency model of the company.³⁶ This theoretical framing of the corporation mandates that it is the primary task of the management to be exclusively accountable to the shareholders and to maximize their profit.³⁷ Consequently, the shareholders must be prioritized in the decision-making process.³⁸ In English law, this theoretical framing of the company is legally embedded in s172 (1) of the Companies Act (CA) 2006, i.e. the duty to promote the success of the company.³⁹ Whilst this duty allow directors 'to have regard to' the interests of various stakeholders, including suppliers, it requires directors to ultimately prioritise the interests of shareholders.⁴⁰

This purpose of the company directly influences the way how company directors engage with CSR in their global supply chain, be it through its own foreign subsidiaries or a network of overseas suppliers. Under this model of the firm, companies will only promote CSR to the extent that it can be based on the business case in the interest of shareholders, i.e. that it promotes the reputation of the

³³ J Ruggie, Introduction to the Guiding Principles, para 14.

³⁴ J Ruggie, 'The construction of the UN "protect, respect and remedy" framework for business and human rights: the true confessions of a principled pragmatist' (2011) 2 *EHRLR* 127, 129.

³⁵ Office of the United Nations High Commissioner for Human Rights, 'New Guiding Principles on Business and Human Rights endorsed by the UN Human Rights Council'.

³⁶ A Johnston, *EC Regulation of Corporate Governance* (CUP 2009) 21

³⁷ S Sheikh and W Rees (eds), *Corporate Governance & Corporate Control* (Cavendish 1995) 10; *Hutton v West Cork Railway Co. Ltd.* [1883] 23 Ch. D. 654, 673.

³⁸ H Hansmann and R Kraakman, 'The end of history for corporate law' (2001) 89 *Geo.L.J.* 439, 449.

³⁹ S172 (1) CA reads as follows: 'A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to – (a) the likely consequences of decisions in the long term, (b) the interests of the company's employees, (c) the need to foster relationships with suppliers, customers and others, (d) the impact of the company's operations on the community and the environment, (e) the desirability of the company maintaining a reputation for high standards of business and (f) the need to act fairly between members of the company.'

⁴⁰ See for a discussion of the duty A Keay, 'The duty to promote the success of the company: is it fit for purpose in a post-financial crisis world?' in J Loughrey (ed), *Directors' Duties and Shareholder Litigation in the Wake of the Financial Crisis* (Edward Elgar 2013) 50.

firm.⁴¹ The voluntary engagement of transnational corporations with CSR in their global production is therefore limited. Rather, transnational corporations focus on the strategic use of foreign subsidiaries and suppliers as a cost-saving instrument.⁴²

2.3. Territorial limits of the law and the legal structure of companies

The violation of CSR principles at factories run by either subsidiaries or suppliers of transnational corporations in the developing world pose a significant challenge due to the territorial nature of the law and the legal personality of companies.

First, the law that is primarily applicable to irresponsible corporate conduct at factories in the developing world such as tort law or criminal law is the law of those countries where the particular incidents have occurred.⁴³ For example, the laws applicable to the Rana Plaza Building collapse are, first and foremost, the laws of Bangladesh. This situation can constitute a challenge where the substantive law of the country where the violation of CSR principles took place has, for example, lower standards in criminal law and tort law.⁴⁴ More often, however, it is not so much the substantive law that is weak in those countries, but rather the law enforcement mechanisms.

Secondly, most transnational corporations do not own the factories that produce for them; rather, the production is done by either foreign subsidiaries which are owned by the transnational corporations or by foreign suppliers. The difference between subsidiaries and suppliers is that subsidiaries are owned by the Western transnational company, whereas suppliers are usually completely independent from the transnational company, i.e. they are owned by other people who are not linked to the transnational corporation. The different ownership structure of the two forms – foreign subsidiaries and suppliers – has also consequences for the liability of the transnational corporation. Supplier companies are legally completely independent companies from the transnational corporation as they are owned by different people. However, there is often a strong economic dependence of the suppliers on the transnational corporation as the buyer of their

⁴¹ See A Kurucz, B Colbert and D Wheeler, 'The business case for Corporate Social Responsibility' in A Crane, A McWilliams, D Matten et al. (eds), *The Oxford Handbook of Corporate Social Responsibility* (OUP 2008) 83 - 112.

⁴² See, for example, The Guardian, 'The Bangladesh factory collapse: why CSR is more important than ever' (7 May 2013), available at <http://www.theguardian.com/sustainable-business/blog/bangladesh-factory-collapse-csr-important> (accessed 22 June 2015).

⁴³ See for an introduction to the idea of 'the law of the place of the tort': D McClean and V Ruiz, *The Conflict of Laws* (8th edn, Sweet & Maxwell 2012) para 12-003.

⁴⁴ Muchlinski notes that the principal jurisdiction level for the regulation of multinational enterprises remains the nation state, see P Muchlinski, *Multinational Enterprises & The Law* (2nd edn, OUP 2007) chapters 3 and 4.

goods.⁴⁵ Their conduct could reflect on the transnational corporation in terms of reputation, but not in terms of legal liability.

Foreign subsidiaries, on the other hand, are linked to the transnational corporation through ownership.⁴⁶ The transnational corporation holds the majority of the shares of the subsidiary, often it is even the sole shareholder, making the other company its wholly-owned subsidiary.⁴⁷ The transnational corporation as the parent company can decide, for example, who the directors of the subsidiary are and it benefits from its profits. However, in English law, even wholly-owned subsidiaries are legal entities which are separate and independent from the parent company.⁴⁸ This is a consequence of the *Salomon v Salomon* principle which has established that companies have a separate legal personality from their shareholders.⁴⁹ This principle has been expanded to corporate groups with the effect that the parent companies are not vicariously liable for the conduct of their subsidiaries.⁵⁰

3. Critical review of existing attempts to regulate CSR in global sourcing

In the absence of binding human rights obligations on transnational corporations in international law, other regulatory mechanisms for the promotion of CSR in the global production have been attempted. Most of these are private governance initiatives which are developed and governed in the private sphere between companies, sometimes involving third parties such as non-governmental organisations.⁵¹ Other regulatory initiatives rely on the home state of transnational corporations such as the US Alien Tort Claims Act (ATCA). This section will critically review these measures in terms of their ability to promote the socially responsible conduct of transnational companies.

3.1. CSR based on private governance schemes

Many transnational corporations with well-known brands are vulnerable to reputational risks and have therefore voluntarily adopted codes of conduct that address the way how they run their business.⁵² Such codes of conduct usually establish principles of good business conduct that the

⁴⁵ See, for example, The Guardian, 'The desperate struggle at the heart of the brutal Apple supply chain' (14 November 2014), available at <http://www.theguardian.com/technology/2014/nov/14/sapphire-gt-advanced--brutal-apple-supply-chain> (accessed 27 June 2015).

⁴⁶ See L Mosley, *Labor Rights and Multinational Production* (CUP 2011) 19.

⁴⁷ S1159 (1) Companies Act 2006.

⁴⁸ See *Adams v Cape Industries plc* [1990] BCLC 479, 513.

⁴⁹ *Salomon v Salomon & Co Ltd* [1897] AC 22, HL.

⁵⁰ B Hannigan, *Company Law* (3rd edn, OUP 2012) paras 3-35 – 3-43.

⁵¹ D Wells, 'Too Weak for the Job: Corporate Codes of Conduct, Non-Governmental Organisations and the Regulation of International Labour Standards' (2007) 7 *Global Social Policy* 51, 52.

⁵² A study published in 2010 shows that 77 out of the 100 constituent FTSE 100 firms had adopted such codes and many companies have policies about ethical sourcing which they integrate into the supply chain relations with their suppliers, see L Preuss, 'Codes of Conduct in Organisational Context: From Cascade to Lattice-Work

company pledges to comply with.⁵³ Transnational corporations increasingly incorporate their code of conduct into their business relations with their suppliers, for example through their supply contracts.⁵⁴ Depending on the way how the principles in the codes of conduct are phrased, they can hereby become contractually enforceable clauses.⁵⁵

At first sight, such private governance regimes appear to be a useful tool to achieve greater socially responsible conduct across the global supply chain of transnational corporations. Through codes of conduct, transnational companies can bind themselves to human rights obligations which are otherwise only contained in international soft law standards.⁵⁶ Moreover, by giving these principles contractual force within their supplier contracts, the transnational companies are able to transcend the territorial limits of law and they can thus impose human rights standards on suppliers in the developing world.

However, despite their widespread use amongst most transnational corporations, private CSR governance regimes have not prevented the repeated violations of human rights at supplier factories in the developing world. Recent examples of irresponsible corporate conduct at supplier factories include the fire at the textile factory Tazreen Fashions in Bangladesh (November 2012), the widespread use of forced labour in the Thai fishing industry (June 2014), breaches of working time and safety equipment provision in the production of electronic devices in China (July 2014), and, most notably, the deadly Rana Plaza building collapse in Bangladesh (May 2013).⁵⁷ All these violations of CSR principles occurred despite the public awareness of human rights breaches in global sourcing and the CSR policies of most transnational corporations.

of Codes' (2010) 94 *Journal of Business Ethics* 471, 475. Preuss analysed the range of codes that constituent firms of the FTSE100 index use. His findings show that 77 companies used a general company-wide code of conduct which often also include stipulations for suppliers, 43 companies had adopted ethical sourcing policies which specifically contain what companies expect from their suppliers in terms of CSR standards.

⁵³ D Wells, 'Too Weak for the Job: Corporate Codes of Conduct, Non-Governmental Organisations and the Regulation of International Labour Standards' (2007) 7 *Global Social Policy* 51, 52.

⁵⁴ A Millington, 'Responsibility in the Supply Chain' in A Crane, A McWilliams, D Matten et al. (eds), *The Oxford Handbook of Corporate Social Responsibility* (OUP 2008) 365.

⁵⁵ A Rühmkorf, *Corporate Social Responsibility, Private Law and Global Supply Chains* (Edward Elgar 2015) 79-125.

⁵⁶ See A Sobczak, 'Are codes of conduct in global supply chains really voluntary? From soft law regulation of labour relations to consumer law' (2006) 16 *Journal of Business Ethics* 167, 168.

⁵⁷ The Guardian, 'Bangladesh textile factory fire leaves more than 100 dead' (25 November 2012), available at <http://www.theguardian.com/world/2012/nov/25/bangladesh-textile-factory-fire>; The Guardian, 'Trafficked into slavery on Thai trawlers to catch food for prawns' (10 June 2014), available at <http://www.theguardian.com/global-development/2014/jun/10/-sp-migrant-workers-new-life-enslaved-thai-fishing>; The Guardian, 'Samsung finds labour violations at dozens of its Chinese suppliers' (1 July 2014), available at <http://www.theguardian.com/technology/2014/jul/01/samsung-working-practice-breaches-chinese-suppliers>; see the coverage of the Rana Plaza disaster by The Guardian, 'Rana Plaza', available at <http://www.theguardian.com/world/rana-plaza> (last accessed 20 June 2015).

Moreover, where the CSR principles have been violated within these private governance systems, the transnational corporations got away with impunity. There is no sanction system such as in state-based regulation that applies in case the CSR principles are not complied with. Companies only have to face reputational concerns. Where the CSR codes of conduct are incorporated into the contracts between transnational corporations and their suppliers, the monitoring of compliance and the enforcement depends on the Western transnational company as the obligations fall on their suppliers.⁵⁸ The workers of the suppliers as the intended beneficiaries of the contractual CSR clauses do not gain any right of enforcement.⁵⁹ And while many transnational corporations have increased their efforts to monitor the compliance of their direct suppliers (also called first-tier suppliers), the majority of violations of CSR principles occur further down the supply chain through subcontracting.⁶⁰ These factories are beyond the reach of the supply chain contracts between the transnational corporations and their direct suppliers which contain the CSR codes of conduct. The private governance based CSR compliance system therefore allow transnational companies to publicly portray themselves as responsible whereas, in reality, subcontracting means that these systems often fail to address those factories where the human rights violations occur.

3.2. The Accord on Fire and Building Safety in Bangladesh: A multi-stakeholder initiative

After the deadly Rana Plaza building collapse serious concerns were raised about the effectiveness of the existing CSR mechanisms in global supply chains. In fact, the building was audited twice by Primark before it collapsed, but the audit did not include a structural survey.⁶¹ This situation illustrates the failure of the existing private governance system of CSR promotion, based on the 'voluntary' inclusion, monitoring and enforcement of CSR by transnational corporations alone.

Due to their failure to prevent the Rana Plaza disaster the transnational companies in the fashion industry which source ready-made garment from Bangladesh were under significant public and political pressure.⁶² In response, the fashion industry came up with different initiatives aimed at improving the situation in Bangladesh. A particularly interesting approach in this context is the

⁵⁸ See A Sobczak, 'Are codes of conduct in global supply chains really voluntary? From soft law regulation of labour relations to consumer law' (2006) 16 *Journal of Business Ethics* 167, 167.

⁵⁹ A Rühmkorf, *Corporate Social Responsibility, Private Law and Global Supply Chains* (Edward Elgar 2015) 102 – 107.

⁶⁰ See G LeBaron, 'Subcontracting is not Illegal, but is it unethical? Business Ethics, Forced Labor, and Economic Success' (2014) 20.2. Spring/Summer Issue, *Brown Journal of World Affairs* 237, 245.

⁶¹ *Vogue*, 'How The World Has Changed Since Rana Plaza' (1 April 2014), available at <http://www.vogue.co.uk/news/2014/04/01/bangladesh-rana-plaza-anniversary-fashion-revolution-day> (accessed 21 November 2014).

⁶² The Guardian, 'Bangladesh pressed on factory safety' (6 June 2013), available at <http://www.theguardian.com/global-development/2013/jun/06/bangladesh-garment-industry-scrutiny-factory-collapse> (accessed 28 June 2015).

Accord on Fire and Building Safety in Bangladesh as a multi-stakeholder initiative.⁶³ Its structure and mode of operation will be critically assessed here in order to discuss whether or not it could be a model for future CSR mechanisms in global sourcing.

The Accord, established in May 2013, is intended to improve the safety of garment factories in Bangladesh. More than two years after its development, in June 2015, the agreement was signed by over 200 apparel brands, retailers and importers from over 20 countries, most of which are from Europe; two global trade unions (IndustriALL and UNI); and eight Bangladesh trade unions and four NGO witnesses such as the Clean Clothes Campaign.⁶⁴ The International Labour Organisation (ILO) acts as the independent chair of the Accord. This initiative covers all suppliers of the companies that have signed the Accord.⁶⁵ It is a five-year legally binding agreement. It stipulates that independent safety inspections must take place at the factories that the signatory companies source from in Bangladesh. The factories are divided into tier 1, tier 2 and tier 3 factories depending on their share of the signatory company's annual production in Bangladesh by volume.

Where flaws are identified the signatory company that sources from this factory is under an obligation to require the supplier factory to implement the corrective actions that were identified by the inspectors.⁶⁶ Additionally, in the event of safety flaws being identified, the signatory companies also commit to ensuring that sufficient funds are available for the corrective actions and that those who work at the factories in question continue to be paid.⁶⁷ The Accord also provides transparency by the regular publication of the list of all suppliers in Bangladesh used by the signatory companies, written inspection reports for all factories inspected under the Accord and quarterly aggregate reports that summarise both aggregate industry compliance data.⁶⁸

The work of the Accord is funded through an annual membership fee paid by the signatory companies which depends on their yearly volume of sourcing from Bangladesh.⁶⁹ The signatory companies commit to maintain their sourcing relationships with Bangladesh. The Accord is governed by a Steering Committee which consists of equal representation chosen by the trade union members and company members of the agreement (maximum three seats each) and a representation from

⁶³ Accord on Fire and Building Safety in Bangladesh, available at <http://bangladeshaccord.org/> (accessed 2 July 2015).

⁶⁴ *ibid*, Signatories.

⁶⁵ *ibid*, Scope.

⁶⁶ *ibid*, Credible Inspection, 9.

⁶⁷ Workers who lose their job as a consequence of working for a factory that is unsafe are promised to be supported, for example, by being offered employment with safe suppliers, see Accord, Remediation, 14.

⁶⁸ *ibid*, Transparency and Reporting, 19. The reports can be found at <http://accord.fairfactories.org/ffcweb/Web/ManageSuppliers/InspectionReportsEnglish.aspx> (accessed 30 June 2015).

⁶⁹ *ibid*, Financial Support, 24.

and chosen by the International Labour Organisation (ILO) as a neutral chair.⁷⁰ Disputes are regulated in the way that, in the first instance, the Steering Committee decides by majority vote within a maximum of 21 days of a petition being filed. By request of either party the decision of the Steering Committee may be appealed to a final and binding arbitration process. The arbitration award is enforceable in a court of law of the domicile of the signatory against whom enforcement is sought.⁷¹

Through the involvement of different stakeholder groups in its governance structure and through the provision of remedial action, the Accord goes beyond the previous attempts to promote CSR standards at factories in the developing world. The Accord is a clear improvement as it does not rely on the transnational corporations alone. It can therefore be argued that future credible approaches to better promoting CSR principles in global supply chains should build on these positive features of the Accord.

However, the Accord has several weaknesses. First, it does not have universal reach amongst transnational companies in the textile industry. Its signatory companies are primarily European textile companies whereas the majority of US-American companies that source ready-made garment from Bangladesh did not agree to this initiative.⁷² Instead, they created the Alliance for Bangladesh Worker Safety which relies on a voluntary, business-driven scheme structure.⁷³ In effect, the Alliance, by and large, continues to operate in the same way as the companies have addressed CSR prior to Rana Plaza. Secondly, the Accord is a five-year plan with no clarity yet what is going to happen after its expiry date. It is quite possible that the signatory companies involved might then declare that sufficient improvements have been made so that, in their view, the scheme would not need to be renewed. It is not sure how much interest the public will take in the issue in a few years' time. Thirdly, the Accord is only a single-issue initiative that is restricted to one country. It is a reaction to a much reported disaster as companies felt the pressure to publicly demonstrate commitment to engage with the cause of the factory collapse, i.e. the poor health and safety standards at factories in Bangladesh. It is important to bear in mind that global supply chains with poor health and safety

⁷⁰ *ibid*, Governance, 4.

⁷¹ It is also subject to The Convention on the Recognition and Enforcement of Foreign Arbitral Awards (The New York Convention) where applicable.

⁷² The Guardian, 'Major US names missing as retailers sign deal to improve Bangladesh safety' (8 July 2013), available at <http://www.theguardian.com/business/2013/jul/08/retail-bangladesh-factories-improve-safety-deal> (accessed 26 June 2015).

⁷³ Alliance for Bangladesh Worker Safety, available at <http://www.bangladeshworkersafety.org/>; The New York Times, 'Battling for a Safer Bangladesh' (21 April 2014), available at http://www.nytimes.com/2014/04/22/business/international/battling-for-a-safer-bangladesh.html?_r=0 (accessed 23 June 2015).

standards exist in many other countries of the developing world, too.⁷⁴ Moreover, the violations of CSR principles in global supply chain is not restricted to health and safety breaches alone; there are many other pressing issues that urgently need to be addressed, too, such as the use of forced labour.⁷⁵ Finally, first reports about the effectiveness of the Accord indicate that the initiative does not cover the large-scale subcontracting that it still taking place in the industry.⁷⁶ The inspections ‘fail to address the greatest risks of this system’ which occur further down the supply chain.⁷⁷

Two years after Rana Plaza and the development of the Accord, transnational corporations have still not worked together to create similar multi-stakeholder initiatives for other CSR issues and other countries. This situation shows that though the Accord is an improvement of the pre-Rana Plaza world, we are still far from witnessing a new era in the promotion of CSR.

3.3. Tort law: The liability of the parent company

Due to the challenges that many tort victims of foreign subsidiaries and suppliers experience with access to justice in their home countries, there is an ongoing discussion about the tortious liabilities of transnational corporations that source from factories where CSR principles are violated.⁷⁸

Companies are liable in tort through vicarious liability.⁷⁹ This is not a tort in its own right, but a rule of responsibility which means that the company is liable for the actions of other people such as employees.⁸⁰

The prospect of making claims against the transnational corporation at the head of the global supply chain is attractive for the promotion of CSR as these companies usually have better financial means and are based in Western countries which often provide easier access to justice. Moreover, transnational corporations with well-known brands are concerned about the reputational damage that results, for example, from losing a case linked to human rights violations. It is exactly for these reasons that transnational corporations are commonly strongly opposed to be subjected to claims by

⁷⁴ See, for example, The Guardian, ‘Improving worker conditions in the global supply chain is good business’ (7 August 2013), available at <http://www.theguardian.com/sustainable-business/improve-worker-conditions-supply-chain-china> (accessed 27 June 2015).

⁷⁵ A Crane, ‘Modern Slavery as a Management Practice: Exploring the Conditions and Capabilities for Human Exploitation’ (2013) 38 *Academy of Management Review* 49, 56.

⁷⁶ S Labowitz and D Baumann-Pauly, *Business as Usual is Not an Option* (NYU Stern Centre for Business and Human Rights, April 2014), available at http://www.stern.nyu.edu/sites/default/files/assets/documents/con_047408.pdf (accessed 24 June 2015).

⁷⁷ *ibid.*

⁷⁸ See, for example, M Anderson, ‘Transnational Corporations and Environmental Damage: Is Tort Law the Answer?’ (2002) 41 *Wasburn Law Journal* 399.

⁷⁹ P Giliker and S Beckwith, *Tort* (4th edn, Sweet & Maxwell 2011) para 7-022.

⁸⁰ D French, S Mayson and C Ryan, *Mayson, French & Ryan on Company Law* (28th edn, OUP 2011-12) para 19.7.2.

victims of torts committed at the factories of their subsidiaries and suppliers.⁸¹ However, the structure of global supply chains makes it difficult to hold transnational companies liable. Although companies can be sued for torts committed by other people, the challenge for legal liability for the relevant torts here is that they occur at factories operated by subsidiaries and suppliers abroad. In the case of suppliers, this situation means that the tort is committed by a company which is legally completely separate from the transnational corporation as there is no link between the two through ownership.

Even where the torts are committed by the foreign subsidiaries of transnational corporations, the tort victims do not have a cause of action against the transnational corporation in English law either.⁸² All companies in a group of companies are separate legal entities, even in case of wholly-owned subsidiaries with only little paid-up share capital and a board of directors which predominately or solely consists of directors who are also directors of the parent company.⁸³ Corporate group structures enable parent companies to reduce their liability risk in tort.⁸⁴ The consequence of this approach is that tort victims of a subsidiary company might not be able to recover their loss, if the subsidiary is undercapitalised.⁸⁵ In *Adams v Cape Industries plc*, the Court of Appeal applied a strict approach to the question of piercing the corporate veil in corporate groups and dismissed the idea of a single economic unit between the parent company and its subsidiaries.⁸⁶ The court held that the corporate veil could in only be pierced where special circumstances exist which indicate that the corporate veil is a mere façade concealing the true facts, i.e. where the corporate structure is used to evade rights of relief that third parties may in the future acquire.

Slade LJ noted:

There is no general principle that all companies in a group of companies are to be regarded as one. On the contrary, the fundamental principle is that “each company in a group of companies (a relatively modern concept) is a separate legal entity possessed of separate legal rights and liabilities”: see *The Albazero* [1975] 3 All ER 21, 28.⁸⁷

Slade LJ also stated that the use of the corporate group by a parent company as a means to ensure that legal liability in respect of future activities of the group will fall on another member of that group

⁸¹ An example of the opposition by businesses is the lobbying in the USA against the Alien Tort Claims Act (ATCA). See D McBarnet and P Schmidt, ‘Corporate accountability through creative enforcement: human rights, the Alien Torts Claims Act and the limits of legal impunity’ in D McBarnet, A Voiculescu and T Campbell, *The New Corporate Accountability: Corporate Social Responsibility and the Law* (CUP 2007) 175.

⁸² See *Adams v Cape Industries plc* [1990] BCLC 479, 513.

⁸³ See B Hannigan, *Company Law* (3rd edn, OUP 2012) para 3-35.

⁸⁴ *Ibid*, para 3-44.

⁸⁵ S Lo, ‘Liability of directors as joint tortfeasors’ (2009) 2 *Journal of Business Law* 109, 120.

⁸⁶ See *Adams v Cape Industries plc* [1990] BCLC 479, 513.

⁸⁷ *Ibid*, 508.

was 'inherent in our corporate law'. The consequence is that the risk is allocated to the poorer risk taker, the tort victim.⁸⁸ This approach does not only disregard the fact that it puts tort victims as involuntary creditors at a severe disadvantage; it also overlooks that limited liability was developed in the 19th century to promote business activities by investors, whereas nowadays parent companies strategically use corporate group structures with a range of (foreign) subsidiaries as an instrument to reduce their liability risks.⁸⁹ Moreover, the rejection of the idea of group liability ignores the economic realities of corporate groups. Parent companies usually maintain close ties with their subsidiaries and they effectively control the running of these companies. The parent companies therefore benefit from the gains made by the subsidiaries whilst they avoid liability for their obligations. English law is also not coherent in its strict application of the *Salomon v Salomon* principle as parent companies must prepare group accounts pursuant to s399 (2) CA 2006.⁹⁰

This approach of English courts to group liability constitutes a significant challenge for the promotion of CSR, as tort victims are unable to make a claim against the transnational corporation as the parent company for the torts committed by its foreign subsidiaries. It is argued here that this approach needs to be changed in order to promote greater social responsibility of transnational corporations. The strategic use of subsidiaries to limit their liability risks contributes to the irresponsible conduct that continues to occur at factories in the developing world.

A potentially different avenue to address the same issue is to hold transnational corporations primarily liable in tort for the working conditions at the factories of their subsidiaries. In the case *Chandler v Cape plc* it was held that a parent company can owe a primary duty of care in negligence to the employees of its subsidiary.⁹¹ In this case, the defendant company *Cape plc*, as the parent company, was directly and jointly liable with its subsidiary (which had been dissolved in the meantime) in negligence for asbestos-related injuries inflicted on the subsidiary's previous employee (the claimant). Prior to this decision, there had been a longstanding debate about the question of whether or not such a primary duty exists in English law, but this issue was never formally decided by a court as the cases were either settled or struck out for other reasons.⁹² The difference between this case and the previous discussion about group liability is that, in *Chandler v Cape plc*, the parent company was held to have breached a duty of care which it directly owed to the employees of its subsidiary company. This duty of care was imposed on the parent company on the basis of an

⁸⁸ P Muchlinski, 'Limited liability and multinational enterprise: a case for reform?' (2010) 34 *Cambridge Journal of Economics* 915, 918, 923.

⁸⁹ S Baughen, 'Multinationals and the Export of Hazard' (1995) 58 *Modern Law Review* 54, 70.

⁹⁰ S404 CA2006.

⁹¹ [2012] EWCA Civ 525 which affirms [2011] EWHC 951 (QB).

⁹² However, it was already argued in the academic literature that a parent company could owe a primary duty of care to tort victims of its affiliates. See, for example: J Zerk, *Multinationals and Corporate Social Responsibility – Limitations and Opportunities in International Law* (CUP 2006) 216.

assumption of responsibility as the parent company had superior knowledge of the asbestos-related risks that the employees of its subsidiary were exposed to. Moreover, it dictated the overall health and safety policy of its subsidiaries and it also exercised control over their business behaviour to an extent that it had the ability to intervene.

The imposition of a direct duty of care on the parent company is distinct from any question of piercing the corporate veil as this approach respects the separate legal personality of the two companies. Rather, parent companies are liable for their own failure to protect the employees of its subsidiaries which resulted in their harm. *Chandler v Cape plc* sets an important precedent for the legal responsibility of parent companies as it restricts the ability of parent companies to completely outsource their liability where they clearly have superior knowledge and are the dominant force within the group. However, it is unclear to what extent this precedent which concerned a particularly dangerous industry related to asbestos might be applied to other business areas and to cases between UK-based transnational corporations and their foreign subsidiaries as the facts underlying this decision occurred in the UK.

3.4. Tort law: The US Alien Tort Claims Act

Whilst this chapter focusses on English law in its jurisdictional scope, it is important to briefly consider the US Alien Tort Claims Act (ATCA) in this context as this statute has, for some time now, captured the interest of those interested in home state liability of transnational corporations for torts committed abroad.⁹³ This Act is, so far, the most successful example of holding parent companies liable in tort law.⁹⁴ The ATCA was enacted in 1789, but only re-discovered and creatively used by NGOs during the late 20th century. The ATCA confers jurisdiction on the US District Court in respect of 'any civil action by an alien for a tort only, committed in violation of the law of nations or a treaty of the United States'. Parent companies based in the USA can be held accountable for human rights violations by their subsidiaries abroad under the ATCA.

In *Filartiga v. Pena-Irala* the court decided that non-American citizens could be punished for tortious acts committed outside the United States which were in violation of public international law or any treaties to which the United States is a party.⁹⁵ This decision is important as it extends the jurisdiction of United States courts to tortious acts committed around the world. A further significant step for the

⁹³ See, for example, D McBarnet and P Schmidt, 'Corporate accountability through creative enforcement: human rights, the Alien Torts Claims Act and the limits of legal impunity' in D McBarnet, A Voiculescu and T Campbell, *The New Corporate Accountability: Corporate Social Responsibility and the Law* (CUP 2007) 148.

⁹⁴ A discussion of the Act can be found at A de Jonge, *Transnational Corporations and International Law: Accountability in the Global Business Environment* (Edward Elgar 2011) 99 – 106.

⁹⁵ 630 F 2d 876 (2d Cir. 1980).

use of the ATCA was the decision in *Sosa v Alvarez*.⁹⁶ Here, the US Supreme Court allowed courts to hear claims by private individuals for breaches of international law committed in other countries. These decisions were followed by a significant increase of claims against US parent companies. However, the courts have been reluctant to assume jurisdiction in cases where the claimants were not resident in the United States.

At present, the future use of the ATCA for tort liabilities of parent companies for tortious acts committed outside the United States is uncertain. In *Kiobel v Royal Dutch Petroleum Co.* the Supreme Court decided in April 2013 that the Act would only apply to conduct within the United States or on the high seas.⁹⁷ It would not create jurisdiction for a claim regarding conduct that occurred in the territory of a foreign sovereign. This decision effectively means that a presumption against extraterritoriality applies to claims under the Act. After this decision it is unclear if the ATCA will play a significant role for liability related to torts committed at factories of foreign subsidiaries of US transnational corporations. This development is unfortunate as the Act was able to fill an accountability vacuum.

Notwithstanding the decision in *Kiobel*, there is, at the time of writing, ongoing litigation under the ATCA concerning the use of forced labour at cocoa firms which supply the confectionery industry. In September 2014, a US appeal court held in *Doe v Nestle USA Inc. et al.* that the claimants were allowed to amend their claim against Nestlé, ADM and Cargill so that the defendant companies could be held to account for aiding and abetting child slavery in Ivory Coast.⁹⁸ The court reinstated a lawsuit filed by three citizens of Mali in 2005 who claim that they were forced to work as child slaves on cocoa plantations in Ivory Coast. This judgment overrules a previous decision by a district court which had dismissed the case on grounds that US courts had not jurisdiction for abuses committed by companies outside the territory of the US. The court held in this case that at least parts of the act occurred in the United States. It remains to be seen, however, how the case is finally decided seeing in light of *Kiobel*.

In summary, tort law is, at least in theory, an attractive avenue for the promotion of greater social responsibilities of transnational corporations as it provides remedies for tort victims. However, changes are necessary for English tort law to better promote CSR in global sourcing, for example group liability would be a strong incentive for transnational companies to use their power to improve working conditions at their foreign subsidiaries.

3.5. Extraterritorial criminal liability: The model of the Bribery Act

⁹⁶ 542 US 692 (2004).

⁹⁷ 133 S.Ct. 1659 (2013).

⁹⁸ 10-56739 (9th Cir. Sept. 4, 2014).

Criminal law is another area of the law that has much potential to improve the working conditions in the global production chain of transnational companies. English law applies criminal law to corporations.⁹⁹ Where corporations are criminally liable, the requirements of the criminal act (*actus reus*) and the criminal mind (*mens rea*) are found in a person acting on behalf of the corporation such as the relevant officer.¹⁰⁰ As companies cannot be imprisoned, they are, if convicted, sanctioned with a monetary fine. Like tort law, criminal law is, first and foremost, bound to the territory of the jurisdiction where the crime occurs.¹⁰¹ Generally speaking, where crimes are committed at factories in the developing world, the crime is prosecuted under the laws of that jurisdiction. The advantage of criminal law vis-à-vis tort law is that the prosecution is initiated by the state. It does not depend on the action being brought by a private individual and therefore, by definition, has a broader reach than tort law. Moreover, the threat of criminal conviction acts as a strong deterrence, not just because of the financial consequences of convictions, but also because of the reputational concerns.

Extraterritorial criminal liability of transnational corporations in their home state is therefore an attractive idea to better promote CSR in global sourcing. In English law, this approach has been introduced in the UK Bribery Act 2010. Common to all cases of bribery in the Bribery Act is the offer or taking of a 'financial or other advantage'.¹⁰² The Act has a near-universal jurisdiction. This approach makes it possible to prosecute an individual or a company with links to the United Kingdom, regardless of where the crime occurred. In particular, the Act makes it an offence for commercial organisations which have business in the UK to fail to prevent bribery by a person associated with it.¹⁰³ The associated person can be an employee, agent, subsidiary or supplier.¹⁰⁴ However, the Act also provides a defence for a commercial organisation if it can prove that it had adequate procedures in place designed to prevent persons associated with it from undertaking such conduct.¹⁰⁵ The government has published guidance about what 'adequate procedures' could be.¹⁰⁶ The guidance, inter alia, recommend companies to use due diligence mechanisms such as anti-bribery terms and conditions in their supply contracts.¹⁰⁷

⁹⁹ Hannigan, *Company Law* (3rd edn, OUP 2012) para 3-89.

¹⁰⁰ *ibid.*

¹⁰¹ See the discussion of jurisdiction by P Muchlinski, *Multinational Enterprises & The Law* (2nd edn, OUP 2007) chapters 3 and 4.

¹⁰² G Sullivan, 'Legislative comment: The Bribery Act 2010: Part 1: an overview' [2011] *Criminal Law Review* 87, 89.

¹⁰³ S7 (1) UK Bribery Act 2010.

¹⁰⁴ S8 Bribery Act 2010. S8 (3) stipulates that 'associated person' may (for example) be an employee, an agent or subsidiary. The list is non-exhaustive, as indicated by 'for example'. Suppliers can therefore be an 'associated person' for the purpose of ss7, 8 of the Act.

¹⁰⁵ s7 (2).

¹⁰⁶ s9 (1).

¹⁰⁷ See Ministry of Justice, *The Bribery Act 2010: Guidance about procedures which relevant commercial organisations can put into place to prevent persons associated with them from bribing* (section 9 of the Bribery

The interesting feature of this approach in terms of promoting CSR is that companies can protect themselves against liability through taking active steps to prevent bribery in their supply chain. The risk of liability combined with the defence of 'appropriate procedures' effectively forces companies to take measures aimed at preventing bribery in their supply chain. As the Bribery Act directly addresses the transnational corporations it overcomes the limits caused by the territoriality principle and the separate legal personality. Transnational corporations cannot outsource their legal responsibility for bribery in their supply chain.

However, as this liability only concerns bribery it will not achieve that companies address other CSR issues in their supply chain with the same caution. The range of CSR violations in their supply chain goes beyond the committing of bribery. It is a missed opportunity that the legislator did not follow the model of the Bribery Act for the UK Modern Slavery Act 2015. There was a discussion about how forced labour in the supply chain of UK-based transnational corporations should be addressed in the Act.¹⁰⁸ One of the options discussed was to create criminal liability modelled on the Bribery Act. However, this idea was eventually rejected and, instead, a supply chain transparency clause was included in the Act.¹⁰⁹

3.6. Disclosure: CSR regulation through transparency

Corporate reporting on CSR, both mandatory on voluntary, has grown exponentially over the last years. Based on public pressure and reputational concerns, companies increasingly voluntarily report about their engagement with CSR, including their global supply chains. However, these voluntary reports are often criticised by NGOs for being public relations instruments that are written in rather vague language and that are not verified. At the same time, mandatory reporting requirements have been an increasingly popular instrument for governments to require companies to report on their engagement with their social responsibilities.

In English law, the strategic report¹¹⁰ which was previously the business review¹¹¹ has the purpose of informing members of the company how the directors have performed their duty under section 172 CA (duty to promote the success of the company). As this duty refers to a range of stakeholders, the strategic report could be an instrument to better promote CSR. In case of a quoted company, the strategic report must, to the extent necessary for an understanding of the development,

Act 2010), (March 2011) para 39, available at: <https://www.justice.gov.uk/downloads/legislation/bribery-act-2010-guidance.pdf> (accessed 24 June 2015).

¹⁰⁸ Joint Committee on the Draft Modern Slavery Bill, Draft Modern Slavery Bill: Report (Session 2013-14, HL Paper 166, HC 1019, April 2014) 85 – 90.

¹⁰⁹ s54 of the Modern Slavery Act 2015. The clause will be discussed in the next section.

¹¹⁰ s414A CA.

¹¹¹ s417 CA.

performance or position of the company's business (a) include the main trends and factors likely to affect the future development, performance and position of the company's business and (b) (i) include information about environmental matters (including the impact of the company's business on the environment), (ii) the company's employees and (iii) social, community and human rights issues, including information about any policies of the company in relation to those matters and the effectiveness of those policies.¹¹² However, if the review does not contain information regarding these issues, it must only state which of these categories it does not contain.

This last sentence of the section shows that quoted companies do not have to report on the range of CSR issues such as human rights in the strategic report as long as they declare that their report does not contain this information. This is a severe limitation for the promotion of CSR. In effect, the reporting about CSR is degraded to a voluntary exercise for directors. Moreover, the law remains very vague about what needs to be included in it. The danger is that directors can comply with their reporting duty even if they make rather neutral statements.¹¹³ Research about the predecessor of the strategic report, the business review, confirms this sceptical view. A study by Villiers and Aiyegbayo, based on semi-structured interviews with key corporate governance actors such as investor relations managers and corporate governance directors from institutional investment firms, showed that the business review made little difference to the quality of reports.¹¹⁴ The authors of this study conclude that companies are struggling to report effectively about their non-financial key performance indicators.¹¹⁵

The continuing debate about the need to require transnational companies by law to be more socially responsible has been taken up by the European Union. A new Directive on nonfinancial information disclosure, adopted in 2014, requires public-interest companies with more than 500 employees to disclose relevant and material environmental and social information in their annual reports from 2017 onwards.¹¹⁶ The Directive stipulates that the annual report of these companies must include a non-financial statement containing information relating to at least environmental, social and employee matters, respect for human rights, anti-corruption and bribery matters.¹¹⁷ This statement must include a description of the policy pursued by the company in relation to these matters, the results of these policies and the risks related to these matters and how the company manages those

¹¹² s414C (7) CA.

¹¹³ C Villiers, 'Narrative reporting and enlightened shareholder value under the Companies Act 2006' in J Loughrey (ed), *Directors' Duties and Shareholder Litigation in the Wake of the Financial Crisis* (Edward Elgar 2013) 108.

¹¹⁴ C Villiers and O Aiyegbayo, 'The enhanced business review: has it made corporate governance more effective?' (2011) *JBL* 699, 712.

¹¹⁵ *ibid.*

¹¹⁶ Article 1 (1) (a) of the Directive.

¹¹⁷ *ibid.*

risks. Companies that do not pursue policies in relation to one or more of these matters shall provide an explanation for not doing so.¹¹⁸

The Directive goes beyond the strategic report as it is more prescriptive and as it applies the 'comply or explain' approach to CSR reporting which means that companies have to give an explanation in case they do not pursue policies. Although the Directive fails to require external verification of the company's CSR reporting, it will expand the quantity of disclosure on those issues by transnational corporations. The Directive can create a level playing field amongst companies across the European Union as it expects companies to have a policy on CSR issues. Still, it remains to be seen to what extent companies are going to use this reporting duty as a genuine opportunity to openly and critically reflect on their CSR policies.

The increasing focus on global supply chains has led to the inclusion of a transparency in supply chains clause in the Modern Slavery Act 2015.¹¹⁹ This clause requires companies of a size that, at the time of writing, is yet to be determined to prepare a slavery and human trafficking statement for each financial year of the organisation.¹²⁰ In order to comply with this reporting duty, companies must either describe the steps that they have taken during the financial year to ensure that slavery and human trafficking is not taking place in any of their supply chains, and in any part of its own business, or make a statement that they have taken no such steps.

The strength of the transparency in supply chains clause is that it recognises the important role of transnational corporations for the eradication of forced labour in global supply chains. However, the clause is rather vague and leaves much discretion to the companies. It fails to establish a requirement that companies must have external third party verification of their forced labour statement. It is likely that, in most cases, companies will be able to continue to report in the same way about how they combat forced labour in their supply chain as they already do in their voluntary CSR report. In actual fact, the transparency in supply chains clause resembles many features of the California Transparency in Supply Chains Act 2010 which, too, requires disclosure on the efforts of a company on combatting forced labour in its supply chain. However, it is also rather soft with no enforcement power and no requirement to have the report externally verified.¹²¹

The various reporting requirements pertaining to CSR issues that have been introduced in the past years demonstrate that, at the moment, the legal regulation of CSR in global sourcing is primarily

¹¹⁸ *ibid.*

¹¹⁹ S54 of the Act.

¹²⁰ Home Office, Modern slavery and supply chains consultation (12 February 2015), available at <https://www.gov.uk/government/consultations/modern-slavery-and-supply-chains> (accessed 2 July 2015).

¹²¹ The Act is available at: http://leginfo.ca.gov/pub/09-10/bill/sen/sb_0651-0700/sb_657_bill_20100930_chaptered.html (accessed 15 February 2015).

transparency laws. Whilst these initiatives are positive steps towards recognising that transnational corporations have social responsibilities for the working conditions at the factories of their foreign subsidiaries and suppliers, they all lack stringency.

4. Conclusion

Recurrent reports about irresponsible corporate conduct by foreign subsidiaries and suppliers of Western transnational corporations demonstrate that the mainly voluntary, business-driven, private governance regime of CSR in global production chains has failed. Transnational corporations are able to hide behind their foreign subsidiaries and suppliers. The division between the corporate headquarters in the global North and West and the production in the developing world presents challenges for the law to adequately address the violations of CSR principles. Transnational corporations outsource both the production and the legal responsibility. Whilst foreign subsidiaries already pose a significant challenge for holding transnational corporations as the parent companies legally accountable, this situation is even more difficult in case of suppliers which are owned by third parties.

Despite its weaknesses, the Accord on Fire and Building Safety in Bangladesh as multi-stakeholder initiative displays some features that future CSR regimes should build on such as its inclusion of different stakeholder groups and its access to remedies. However, two years since its development, no similar scheme for other countries and other CSR issues has been developed. The danger is that the Accord remains a single-issue initiative that resulted from significant public and political pressure in the wake of the Rana Plaza disaster.

In the absence of a binding international human rights framework for transnational corporations, there is a growing consensus that the home state of transnational corporations has got a more important role to play in the promotion of CSR. The home state could fill some of the legal loopholes of global sourcing. However, at present, the regulation of CSR issues is focussed on disclosure laws which are not stringent enough to ensure that transnational corporations go beyond their present efforts. The chapter has shown that tort law and corporate criminal law could be an important part of the legal promotion of CSR, as they have the potential to hold transnational corporations legally accountable for irresponsible conduct at factories run by subsidiaries and/or suppliers. However, in order to use their full potential, both areas need amendments in English law.