ELENA GILARDI*

Contractualization of sustainability goals

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1. Whereas

A key area of corporate social responsibility (CSR) is the extent to which in the globalization phenomenon companies manage their supply chains responsibility. In other words how they ensure their chains of suppliers and/or subsidiaries respect basic rights (from labors such as decent work, freedom of association, health and safety at work) to more ethical and social rights (such as respect for the environment and of local communities).

The historical development of the concept of sustainability proves that the *contactualistion* of sustainability goals reflects nowadays globalized economy based on Multinational Enterprises and their supply chains.

In fact, Multinational Enterprises in addition to corporate codes of conduct, are implementing into their models of commercial agreements (e.g. international investment and supply chain contracts) another private and soft tool for promoting social, ethical and environmental accountability: the sustainability contractual clauses (hereinafter "**SCC**").

The aim of this article is to review the regulatory effects of these clauses over the suppliers, and the remedies in case of breach trying to reply to the following question: are these contractual clauses effective and enforceable? After an analysis of some case studies the conclusion reached is that, as in case of codes of conduct, the enforceability and

* Giurista di impresa/In-house lawyer with a LLM in International Contract Law.

binding nature of SCC depends on the formulation and language specificity of the relevant provisions, on the ways to dissuade the counterparty from breaching such clauses (e.g. termination clause; contractual penalties; a refusal to source again) as well as on the monitoring mechanisms used for ensuring compliance with them (e.g. transparency of the external audit's report; *ad hoc* committee set up by the parties; database of compliant counterparties).

2. Definition and historical development of the concepts of sustainability

Corporate Social Responsibility (CSR) is defined as operating a business on a reliable, sustainable and desirable basis that respects ethical values, people, communities and the environment[1].

The term "sustainability" comes from "sustainable development" which was coined in the paper *Our Common Future*, released by the World Commission on Environment and Development in 1987. In the so-called "Bruntland Report" sustainable development is defined as the "*development that meets the needs of the present without compromising the ability of future generations to meet their own needs. It contains within it two key concepts: the concept of needs, in particular the essential needs of the world's poor, to which overriding priority should be given; and the idea of limitations imposed by the state of technology and social organization on the environment's ability to meet present and future needs".*

For any organization to be sustainable in the long term, it firstly needs to be financially self-sufficient. Once this primary need for financial capital has been met, the organization then needs to be socially responsible. This explain why the development of CSR –type of activities is connected with the regular progress over the past decades of globalization and the growth of Multinational Enterprises[2].

In fact globalization causes the weakening role and power of states. In parallel, globalization gives more power and resources to private

[1] Anderson, J., W., (1989), *Corporate Social Responsibility*, Greenwood Press, Connecticut.

[2] Scherrer, Andreas Georg and Guido Palazzo (2009). *Globalization and Corporate Social Responsibility*. In Crane, Andrew, Abagail McWilliams, Dirk Matten, Jeremy Moon and Donald Siegel (eds), *The Oxford Handbook of Corporate Social Responsibility*. Oxford, UK: Oxford University Press, pp. 413-32.

actors – particularly large corporations that operate in multiple countries. In that context, corporations are bound to enter the space deserted by governments – if only to produce some of the institutional rules and public goods necessary to their own proper functioning. CSR hence takes the form of private, public and common good provision.

Key drivers of contemporary CSR are globalization and contemporary corporation characterized by (1) being legal entities which can exist, potentially, in perpetuity, and at least well beyond the life span of their original shareholders; (2) having ownership based on the holding of shares. Corporate ownership tends to be dispersed and shares are easily transferable and marketable; and by (3) having limited liability. Shareholders cannot be made liable for the debts and liabilities of the corporation beyond the value of their holdings.

These peculiar features of the modern corporation have an impact on the ways in which it interacts with its surrounding social contexts. They also shape the sense of social responsibility of these firms and the forms it takes.

3. Multinational Enterprises and sustainable principles - From Codes of Conduct to sustainability contractual clauses

As before noted, economical globalization is promoting greater competition, which has forced corporations to seek decreased production costs by outsourcing production to areas where the cost of labour is still low. Moreover, in many of the developing countries where Multinational Enterprises operate, the rule of law is ineffective, there are no legal remedies, no possibilities of redress and thus it has been claimed that they can act with almost total impunity[3].

Notwithstanding the above, corporations are increasingly expected to perform as political actors in relation to the environment, human rights, working conditions and welfare provisions. While the globalization has given Multinational Enterprises great economic and political power, the powers of the states are constantly declining. Of the world's 100 largest economies today, more than half are corporations

[3] Habbard A.C., *The Integration of Human Rights in Corporate Principles*, in: Organisation for Economic Co-operation and Development, *OECD Guidelines for Multinational Enterprises 2001*, Annual Report, OECD, Paris, 2001, p. 99.

and not countries[4]. Thus, in many social sectors and global regions, corporations are probably able to provide more services and a more sustainable infrastructure than governments.

In addition, the corporate scandals we experienced at the beginning of this century (e.g. Enron, WorldCom and Parmalat) have raised awareness of the broader social impact of corporations and formed the new business environment.

To respond to the global expectations in terms of CSR, Multinational Enterprises have incorporated corporate social accountability standards into their supply chain operations which address various social issues. These standards can be internal voluntary codes of conduct established by the corporation itself or external voluntary standards established by non-governmental organizations. Compared to legislation, self-regulation provides the corporations with a voluntary and flexible tool to address these concerns.

The essential premise is that the code of conducts may force suppliers in the developing world to follow the values and standards set by the western MNCs. When the buyers think that some suppliers are compliant with their code of conduct, they are then willing to place the orders with that specific supplier. However, the code of conducts themselves cannot guarantee compliance. A code can only reveal core values and is not a corporate compliance program in itself. Hence, the two most common critiques of codes of conduct are the inability of corporations to effectively implement the commitments and the lack of monitoring mechanisms.

As before noted, SCCs often refer to the provision(s) about sustainable development provided for in the Code of Conduct of a MNEs. In this respect, certain provisions of the Code of Conduct are subject to a *contractualisation* in the agreements with the MNE's suppliers.

The literature notes that the Codes of Conduct appear in many different forms and they differ by their content, by the monitoring mechanism they may or may not include, and by the level (the individual company, the sector, the country or group of countries) at which they are drafted and proposed for adoption. They appear on company's websites and in annual reports.[5]

[4] See www.corpwatch.com.

[5] Fiona McLeay, "Corporate Codes of Conduct and the Human Rights Accountability of Transnational Corporations: A small piece of a larger puzzle in

The instrument of the Code of Conduct experienced in the last 15 years a great diffusion. Levi-Strauss is usually credited as the first to establish a Code of Conduct with comprehensive principles regarding its global sourcing and operations, in 1991. Nike followed later the same year.

International organizations have often researched about the impact of such instruments in global markets. In particular, in May 2001, the OECD published a review of 246 Codes of Conduct.[6] In 2003, the World Bank estimated them to be around 1,000.[7] The reason for the rise is not only that their implementation may confer competitive benefit to the MNEs helping them in establishing the so-called "social legitimacy" and to clean their image. It also consists in the fact that they are felt as a necessary private tool to fill the gaps where states regulation are present only to a small degree and the solutions provided at international level are undermined by different national interest.[8]

Generally, the Code of Conduct aimed at, among other, describing the principles devoted to manage the business in a sustainable manner. Hence, they are drafted in compliance with the principles established by International Institutions and Conventions and within the framework of the United Nations Universal Declaration of Human Rights, as well as the OECD Guidelines for Multinational Enterprises. It may also rely on the suggestions provided by national authorities such as category associations and trade union representatives concerning fair employment practices, freedom of association, rejection of any form of discrimination, of forced labour, child labour while safeguarding dignity, health and workplace safety.

The obligation to comply to the above sustainable principles in addition to the general duties of loyalty, impartiality and compliance in good faith with their employment contract, is usually incorporated into the same employment contracts or referred to with side letter

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Transnational corporations and Human Rights edited by Olivier De Schutter, Oxford and Portland, Oregon (2006),219.

[6] http://www.oecd.org/daf/inv/investment-policy/WP-2001_6.pdf

[7] http://siteresources.worldbank.org/INTPSD/Resources/CSR/Company_Codes_of_Conduct.pdf

[8] Martin Herberg, "Global Legal Pluralism and Interlegality: Environmental Self-regulation in multinational Enterprises as Global Law-making", in Responsible Business Oxford and Portland Oregon, (2008) 17.

documents**.** Hence, it is imposed to employees the duty to comply with company rules and the prescriptions of the Code of Conduct, whose obedience is required pursuant to and within the meaning of the relevant labour laws.[9]

The scope of the Codes of Conduct has now been extended to include also MNEs supply chains, with more concerns in terms of their enforceability and related monitoring procedures arising thereto. This is the real challenge of this millennium in relation to the increasing usage of the SCCs as a (private and effective) tool promoting a sustainable development.

As emerged by the OECD survey[10], in practice most of the codes contain no real sanction for non-compliance. The survey found few examples of codes where non-compliance would lead to a serious penalty, such as a financial sanction or even termination of a contract. The response to code violations is more likely to be the maintenance of the relationship and attempts to remedy the breach, rather than imposing a penalty on the offending supplier.

In fact, control and monitoring procedures although diverse and varied, have as common feature the fact that they (so far) do not rely on legal and judicial mechanisms, but on mechanisms set by the same companies. Difficulties are also due to the fact that MNEs use complex supply chains. This makes it harder and harder to control each of potentially hundreds of global contractors, subcontractors and suppliers.

MNEs impose such principles, including the goals related to the promotion of sustainability, by including them as a supplier's obligation in corresponding commercial agreements. These principles are usually incorporated into agreements with suppliers, partners, consultants,

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[9] Usually a specific clause is inserted in the employment agreement stating as follows:
"Violation of the provisions of the Code of Conduct constitutes a breach of discipline and of employment contract and, as such, sanctions may be imposed. The Company defines disciplinary actions on ascertainment of violations of the Code of Conduct in accordance with the provisions of the applicable Collective Bargaining Agreement or of the individual contract."

[10] OECD (2001), "Codes of Corporate Conduct: Expanded Review of their Contents", OECD Working Papers on International Investment, 2001/06, OECD Publishing. http://www.oecd.org/daf/inv/investment-policy/WP-2001_6.pdf

agents, dealers, distributors contractors, and any other parties with whom the company is establishing a long-term relationships.[11]

Generally, these obligations have to be followed by the supplier because:

(i) they represent ethical values that supplier commits to respect through representation and warranties;
(ii) they may require a supplier to perform obligations in compliance with stated principle, or
(iii) they may provide environmental practices for the supplier to be followed.

The point here is when the terms of a Code of Conduct are incorporated into an international supply chain agreement (hereinafter "**ISCAs**"), they become legally binding as any other obligations contained in the agreement. Examples of drafted general clauses to be incorporated in the commercial agreement related to the recognition of, and adherence to the fundamental principle of a Code of Conduct, could be:

"***Code of conduct:*** *The Supplier declares to be aware of Company's Code of conduct made available to him and agrees to comply with such code of conduct in all respects while performing its obligations under the Agreement. The Parties agree that the violation of these prohibitions or obligations is deemed as fundamental and hence entails the immediate termination of the Agreement, without prejudice to damages."*

Or

"***Enforceability of Code of conduct***: *In order to ensure that this Code of conduct is applied, suppliers must acknowledge in writing that they have read, understood and accepted this Supplier Code of conduct. Suppliers hereby commit to perform their business activities with the highest level of integrity and compliance within the terms of the Supplier Code of conduct among their staff and throughout their supply chain".*

The incorporation of such provisions of the Codes of Conduct into ISCAs make them formally enforceable, and (as it is commonly provided for) to have the legal right to terminate the contract in case of non-compliance. Contractual parties are free to agree on the contractual content that governs the relationship and can be enforced through formal proceedings.

[11] H. Ward, "Legal Issues in Corporate Citizenship" (IEED, 2003). Accessed (25 March 2015) at http://pubs.iied.org/pdfs/16000IIED.pdf

However, since most of the terms of a Code of Conduct reflects broad values or principles and mostly show a very high level of abstraction, it is difficult to determine whether a supplier has actually failed to comply with them. Thus, there is a risk that domestic courts do not enforce all contractual provisions: for example, vague clauses from which no specific right or obligation can be deduced are usually not enforceable before domestic courts. If an obligation is not clearly stipulated, there may be no breach.

4. Regulatory effects of Sustainable Contractual Clauses over the suppliers

4.1 The enforceability of SCCs obligations in ISCAs

SCCs must become a valid part of a contract in order to be enforced. Concerning contract law, there exist in almost all jurisdiction the principle of party autonomy which allow contracting parties to regulate the terms and conditions of their relationship in full autonomy safe for the so called mandatory rules or - talking about contracts - until the agreement is neither illegal nor immoral.

It derives from the above that companies are legitimate to make those promises concerning its own behaviors by establishing or signing a Code of Conduct, but the problem of the enforcement of said contractual promises and related litigation for breach of promises is yet to be evaluated and to be balanced with specific limits set by national contract law found applicable to the breach of claim.

MNEs and their suppliers should be aware that these provisions may become an integral part of an agreement not only by their direct implementation into the contractual text, but also by reference to another document, such as a Code of Conduct or a soft law instrument.

While express provisions pose less formal problems, the incorporation by reference can sometimes raise concerns as to whether the referenced document becomes validly a part of the contract. For example, a Code of Conduct or any other CSR document may qualify as standard terms and conditions, if one party only in advance of the

contract drafts it and intended it for general and repeated use.[12] In any case, in order to establish if a referenced document became a part of a contract we have to look into the form and content of the reference. International contract law does not provide any specific rules in this respect; therefore, the general rules on interpretation of the parties' intentions will apply. The reference must be made in such a form and language that a reasonable person would comprehend that the mentioned document is intended to form part of the contract. It does not need to be in writing or signed. Furthermore, it does not need to be placed directly in the contractual text, but it can be for example made clear during pre-contractual negotiations.[13] Thus, signing a Code of Conduct by a supplier in the pre-contractual phase, which states that the buyer intends to cooperate only with suppliers fulfilling therein-stipulated requirements, may be interpreted as incorporation of the code as standard terms and conditions into the agreement.

The supplier should be aware of the referenced CSR documents. A mere statement that a supplier must fulfil requirements stipulated in a Code of Conduct is not sufficient; he must be also able to access the text. Except for express provisions or incorporation by reference, some authors argued that sustainability requirements become part of international contracts impliedly, without the necessity of contractual parties expressly acknowledging them. This may happen through the concepts of practices that the parties have established between themselves or international trade usages.

Parties are also bound by trade usages that are widely known and regularly observed by traders involved in the particular trade and of which the parties knew or ought to have known. Some authors suggest that observance of ethical standards constitutes such an international trade usage.[14] However, we note, the scope of the obligations that would

[12] UPICC art 2.1.19; PECL art 2.209 (3); CESL art 2 (b); the CISG does not contain a special provision on standard terms and conditions.

[13] S. Vogenauer and J. Kleinheisterkamp (eds), *Commentary on the Unidroit Principles of International Commercial Contracts (PICC)* (OUP 2009), art 2.1.19, para 13.

[14] I. Schwenzer and B. Leisinger, B., 'Ethical Values and International Sales Contracts', in Ross Cranston, Jan Ramberg, Jacob Ziegel, J. (eds) Commercial Law Challenges in the 21st Century: Jan Hellmer in memoriam (Iustus Forlag 2007) 249.

fall under the usage is not clearly established and thus this would not be sufficient for the enforceability of such clauses.

4.2 Contractual remedies

Contract termination may play an important role also with respect to SCCs: a refusal to source from a supplier is considered as the most severe punishment. Although contract termination is a remedy provided to a buyer under all international contract law instruments, it is most often executed outside of any formal enforcement proceedings; a company may simply stop placing orders to the supplier.

If it comes to a formal disagreement about the right to terminate, the court would have to establish whether the breach in question amounted to a fundamental breach. This is easy if the contract states that non-compliance with SCCs constitutes a fundamental breach, but much more difficult if it does not. Usually, a fundamental breach is found when the main obligation under a contract is not fulfilled. A breach of ancillary obligations can also result in a fundamental breach, but most probably not if those obligations were not connected to the goods' non-conformity.

A fundamental breach must also be foreseeable according to the general rules on contract interpretation. The main aspect to examine in this respect will once again be the language of the SCCs and/or the manner in which the supplier was informed of the buyer's CSR standards. Therefore, it can be concluded that the possibility of contract termination plays an important role in the use of SCCs, but the role relates more to the deterrence function of such a provision than its actual use. In this sense, underlying contract law is crucial in allowing multinational buyers to exert legal pressure over their suppliers.

In fact, terminating the relationship although appearing as the suitable legal tools against supplier's violation for principles embedded in the codes of conduct could be detrimental for the company, which will lose the investments into the relationship and needs to build a new one. Moreover, terminating the agreement does not help to recover the damages for bad reputation. Finally, should the supplier contest the termination, it may be difficult to prove that a breach of a Sustainability contractual provision constituted a fundamental breach of the contract.

The other two typical contractual remedies next to contract termination - specific performance and damages – should also be considered.

Specific performance actually cannot be used in relation to SCCs, since these requirements do not relate to the physical product quality. The courts have been reluctant to recognize CSR production method-related requirements as product characteristics in consumer cases, and it can be expected that the same would happen in business cases as well.

Because the most common and probably the most detrimental consequence of suppliers' breach is the buyer's damaged reputation, specific performance is inconsequential, because the buyer cannot recover the loss suffered.

In order to claim damages under international contract law the buyer then has to prove a breach, damage that was foreseeable and a causal relationship between the two. All may pose problems in relation to SCCs. Firstly, a breach can occur only where there is a binding obligation. As discussed earlier, the binding nature of SCCs is dependent on the relevant provision's form and specificity. Secondly, if an SCC is breached, most likely a non-pecuniary damage occurs, usually a reputational harm. Whereas UPICC and PECL expressly provide for the possibility of recovering non-pecuniary loss[15], the same is the subject of an academic discussion and contradicting court decisions under CISG and it is expressly excluded in relation to reputational loss by CESL.[16]

Finally, the causal relationship between breach of an SCC and relevant damage will often be a controversial matter and it will be even harder if a buyer claims a future loss, which must be proved with reasonable certainty. It may be impossible to reach reasonable certainty, unless the buyer for example faces litigation by third parties due to the breach in question and expects to lose it.[17]

Thus, claiming damages might be more helpful for the buyer, but establishing a link between the supplier's breach and any loss suffered by the buyer may be difficult. Furthermore, calculating damages is

[15] UPICC art 7.4.2(2); PECL art 9:501(2)(a).

[16] P. Schlechtriem, "*Non-Material Damages – Recovery Under the CISG*?" (2007) 19 Pace Int'l L.Rev. 89. Reputational damage is excluded; see at CESL, regulation proposal art 2(c).

[17] Schlechtriem, *supra*.

problematic. Damages often include non-monetary damage such as future loss of profit due to harmed reputation.

Finally, remedies under contract law are not suitable for the purposes behind social and environmental provisions, namely reputational protection and risk management.

4.3 Relational enforcement tools

Given their nature of relation tools, SCCs' enforcement is primarily based on relational enforcement tools.

First of all, monitoring, because non-compliance is not detectable after the goods are delivered. For example, we cannot see from the goods' appearance that children were used to produce it. The majority of companies use suppliers' self-assessment to start with. It is often required during the suppliers' selection process as a part of risk assessment and due diligence as well as during the contractual term. As a cheap although highly subjective alternative, self-assessments can be conducted often and commonly serve as detecting 'red flag' issues, which are then further followed up by suppliers' audits. A variety of audits exists, including internal and external, announced and unannounced audits on site, audits coordinated among groups of firms and according to different audit standards. Each type has some associated positives and negatives, but all of them face a common criticism pointing towards unreliable and subjective results and corruption practices.

In response to the criticism, companies are becoming more transparent about the audit results. This information, despite its possible incompleteness, is essential for implementing any practical change in suppliers' behaviour through various soft and hard remedial strategies. If non-compliance is discovered, the buyer will usually work with the supplier to find solutions.

For example, the most common tool that companies use is a so-called corrective action plan, under which the parties agree what the supplier must do to remedy the breach. Sometimes, the buyer will even provide a supplier with capacity building resources, such as training or assistance. The aim of these relational strategies is to secure compliance with sustainability requirements in a collaborative manner and avoid disputes. It is common that buyers expect a certain level of non-

compliance among their suppliers and thus do not break off cooperation if a supplier is willing to improve.

In addition to the positive relational enforcement tools, companies may also rely on name-and-shame strategies. An increasing number of CSR initiatives establish a database of compliant suppliers. Members of the specific initiative can no longer use a supplier, who is erased from such a database or, worse still, listed as noncompliant.

Relational enforcement tools are essential for the effectiveness of SCCs as they aim to actually change behavioural patterns in supply chains. However, although neither companies nor regulators stress it, the effectiveness of the relational tools is grounded in the threat of formal legal sanctions. This reliance on the indirect enforcement power of formal legal sanctions is evident from the frequent reservation of the right to terminate a contract if the supplier's non-compliance is not remedied.

4.4 Case studies

Some MNEs, and also third parties to contracts, have tried to enforce suppliers' breach to comply with SCC - in order to respond to the lack of internal sanctions for code breach - indirectly using the tools of consumer law (misleading advertising)[18], labour law or contract law.

However, no case (so far) against a company for breach of a code has reached trial on the substantive issues. Most, such as the Nike case (described below), settled the disputes before entering into the substantive claims. This seems to confirm that MNEs more often use the relational remedies (see before) in case of non-compliance of their suppliers.

Moreover, in term of enforceability, it is worth to mention that the wording of the codes does not always give clear answer to the question whether they will prevail over local law or practice at the place of

[18] For reference to certain case-studies involving German law please refer to Eva Kocher, "Codes of Conduct and Framework Agreements on Social minimum Standards. Private regulations?" in Responsible Business Oxford and Portland Oregon (2008), 67. They refer to cases where the company promotes its products on the basis that they were produced in compliance with certain minimum social standards arising in Misleading advertising in violation of section 5(1)(2) of the German Act against Unfair Competition.

production, or if the interpretation of national law will rather determine the interpretation of the standards.

As pointed out in the literature[19], the evaluation of the effectiveness of codes of conducts is not yet been exploited in a consistent way primarily due to lack of empirical studies. This is due to the fact that the Codes of Conduct are private instruments and therefore there is little transparency in their development and implementation by MNEs and only those been brought to the attention of the public for the attack or criticism by the media are known and analyzed (see for example the Nike case[20]).

Moreover legal actions arising therefrom (especially in the US in the form of a class action) ends with settlement agreements which do not include any admission of liability by the companies.[21]

Good example of legal actions ending with no liability since the cases were settled before the final judgment is represented by three separate lawsuits filed in 1999 in Californian state and federal courts and in a US federal court on the West Pacific island of Saipan against a number of US clothes retailers and against garment contractors based in Saipan. Saipan is exempt from US immigration and minimum wage laws. The legal actions were brought by NGOs and a class of some 30,000 foreign textile workers, most of whom had been brought from China and the Philippines by apparel companies to work in their factories in Saipan. Some workers were forced to pay recruitment fees in their home countries. These fees effectively tied people to their employers in Saipan to pay back the debt. A first legal action alleged breaches of Californian state law on unfair business practices on the basis that the defendant companies had falsely advertised their goods as sweatshop free, and aided and abetted violations by their contractors in Saipan of laws against involuntary servitude as well as other misleading labelling and advertising practices. A second action was based on federal laws: the Alien Tort Claims Act, the Anti-Peonage Act, which prohibits use of forced labour, and RICO – the Racketeer Influenced and Corrupt Organizations Act. To state a claim, plaintiffs must allege unlawful conduct of an enterprise

[19] Fiona McLEAY, cited above, 224.

[20] See for example *Kasky v. Nike*, 45 P.3d 243 (Cal. 2002), where Nike has been challenged for accountability not only for the activities carried out by the manufacturers but also for their suppliers' and subcontracted factories.

[21] H. WARD, cited above 17-18.

through a pattern of racketeering activity violating specified 'predicate acts,' which include involuntary servitude and indentured labour. RICO broadly defines 'enterprise' to include 'any union or group of individuals associated, in fact, although not a legal entity.' The plaintiffs' alleged that the defendants' behaviour amounted to a pattern of racketeering activity, which exists when a person commits or aids and abets two or more specified acts that have sufficient continuity and relationship so as to pose a threat of continued criminal activity. The substantive legal principles at stake in the case have not been tested, since settlement talks began early in the action.

The cases of Nike Inc., SKF, Ocean Trawlers and Ikea also deserve attention.[22]

Kasky v. Nike

The Kasky v. Nike case, probably the most known case study, originates from the lawsuits brought by the environmental activist Marc Kasky claiming that the statements - made by Nike in response to alleged non ethical labour practises in its supply chain[23] - to work worldwide in accordance with a strict code of conduct, free from sweated labour, were false or misleading, and that they should be censured under California's unfair competition legislation and false advertising.[24]

The action challenges the accuracy of the report commissioned by Nike on compliance with its corporate code by suppliers[25].

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[22] A. Carlsson, *Corporate Social responsibility: the Lex Mercatoria of Corporate Governance in the 21st century*, Stockholm University (2010).

[23] For reference to the Nike's case see Andersen Carlsson, "Corporate Social responsibility: the Lex Mercatoria of Corporate Governance in the 21st century", Stockholm University (2010), 60; H. Ward cited above,19; and Sol Piciotto, "Rights, Responsibilities and Regulation of International Business" 42 Colum. J. Transnat'l L. 131 2003-2004), 146.

[24] Kasky v. Nike, 45 P.3d 243 (Cal. 2002). Overturning decisions of lower courts, the Supreme Court of California held that since Nike's statements were representations of fact about the company's commercial operations, they were commercial speech, and thus not protected by the First Amendment.

[25] The Nike code of conduct: a report on conditions in international manufacturing facilities for Nike, Inc. (1998). The Report was produced by GoodWorks International, LLC, a consulting group chaired by Andrew J. Young, based on Mr. Young's investigations.

Nike cited the US constitution's First Amendment, which enshrines freedom of speech. Notwithstanding the fact that initially, the San Francisco Superior Court and the California Court of Appeal dismissed the action, agreeing with Nike that the company's statements were indeed protected by the First Amendment, in May 2002, the California Supreme Court stated that the company statements amounted to "commercial speech" because they were directed by a commercial speaker to a commercial audience (consumers of Nike products), making representations of fact about Nike's business operations 'for the purpose of promoting sales of its products'. Commercial speech is not subject to the same level of protection as 'political speech' under the First Amendment.

As a consequence, the commercial statements would be subject to the stricter standard of truth required by advertising law. The case was thereafter settled where Nike was to pay $1.5 million to the Fair Labor Association (FLA) to be used for worker development programs and hence no ruling on the found of evidence of illegal or unsafe working conditions at Nike factories in China, Vietnam, and Indonesia has been given.

Notwithstanding the above, from such lawsuits Nike adopted a rather hard-line approach towards suppliers, drawing a sharp line on how much non-compliance will be tolerated before the supplier's contract will be terminated. In general, Nike accepts a maximum limit of three non-conformances before terminating a contract and forever excluding the supplier from their sourcing. This strategy has been criticized as being more about protecting a brand name rather than the supplier's workforce.

SKF

SKF is viewed as one of the most successful company's Code of Conduct because it implements social and environmental activities into its core business plan and recognizes Sustainability projects as one of the corporations' key business drivers.

The SKF´s *Code of Conduct*[26], introduced in 2002, in order to "*enable systematic compliance assessment and risk identification*" is applicable to all of the SKF Group's operations worldwide and has also been used as a reference to establish other documents such as the SKF Code of

[26]See http://www.skf.com/group/supplier-portal/responsible-sourcing/skf-code-of-conduct-for-suppliers-and-sub-contractors/index.html

Conduct for Suppliers and Sub-contractors, and the SKF Code of Conduct for Distributors, demanding similar high levels of commitment from their business partners.

Ocean Trawlers

In 2004 and 2006 Ocean Trawlers (market leader in supplying and processing cod and haddock from the Barents Sea and a leading distributor to Europe, Asia and the U.S.) was involved in a Norwegian and a Swedish TV documentary which accused the corporation of illegal fishing. Although media information turned out to be false, the case shows the importance of traceability and transparency in order to respond to public demands being more prepared to identify risks and respond to allegations.

Ikea

In the early 1990s a Swedish documentary discovered brutal production methods among several suppliers in Pakistan linked to IKEA and a German documentary raised the issue of child labour. Together with other companies, IKEA was cited as a customer of wicker suppliers employing children, causing the corporation to review their supply-chain.

IKEA's current Code of Conduct, *The IKEA Way on Purchasing Home Furnishing Products*, was officially launched in 2000 to secure their sourcing in developing countries such as China in order to better face failure in monitoring its supply-chain processes and therefore increase traceability in the business.

For an analysis of the impact of codes limited to "employee rights" it is interesting to read the conclusion reached by an author [27] reporting on the "Schrange Report"[28] which analyzes four cases related to manufacturing sector in China, demonstrating that according to the context the outcomes of the implementation of the same Code of conducts can vary significantly.

***Adidas*-Salomon**

The analysis involves two factories in China having both implemented the *adidas*-Salomon Code of Conduct used to encompass the activities of the Adidas supply chain. Contractors and companies

[27] Fiona McLEAY, cited above.

[28] E. SCHRANGE, "Promoting International Worker Rights Through Private Voluntary Initiatives: Public relations or Public Policy?", report to US Department of State in behalf of the University of IOWA Center for Human Rights, January 2004.

who contract with *Adidas*-Salomon sign terms of engagement that require them to uphold the Code of Conducts. This is accompanied by educational tools (handbooks and posters) to educate the workers in the factories about the terms of the codes and about the mechanism for bringing complaints for their violation. Responsibility for controlling their implementation is left to the *Adidas*-Salomon Social and environmental Affairs department, which carries out regular visits to supplier to check adherence and to assist in resolving compliance problem.

Notwithstanding the same set of instruments, factory A showed better application of the Code of Conduct and performed also better than factory B, including demonstrating better levels of pay and health and safety, and lower labour turnover, while in factory B the code has been see as one of the conditions needed to be satisfied to continue to do business with Adidas, but the code did not become an integral part of factory's business operation: simpler compliance approach. The better success in factory A can be explained by A's management having successfully interpreted and implemented the Adidas code of labour practice as a collaborative relationships.

5. Conclusion

From the analysis carried out above, it is showed that sustainability compliance in its recent form of sustainable contractual clauses is the result of globalization which is characterized by a weakening role and power of nation states along with more power and resources given to private actors.

Multinational Enterprises are trying to answer to this emerging new call of sustainability principles by inserting internally to their structure and externally in their supply chain obligations to comply with sustainable standards and principles.

Notwithstanding the above, as demonstrated by the case studies perused this partial re-privatization mechanism is facing several challenges.

An open issue remains. Notwithstanding the wording of SCC clause, its provisions are not enforceable throughout the whole supply chain. In fact, the MNE may force compliance only on its direct suppliers but face difficulties in achieving compliance of further supply chain tiers, with whom MNE has no a direct business relationship.

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