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Roundtable on Corporate Responsibility: Supply chains and the OECD Guidelines for Multinational Enterprises

SUMMARY OF THE ROUNDTABLE DISCUSSION

19 June 2002

This document reproduces the summary of the Roundtable discussion which was held on 18 June 2002. It will form part of the forthcoming publication "OECD Guidelines for Multinational Enterprises -- Annual Report 2002".

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The OECD Roundtable on Corporate Responsibility is held every year in conjunction with the annual meeting of the National Contact Points (NCPs). The second Roundtable dealt with the issue of supply chain management and was held on 19 June 2002. In opening the Roundtable, Deputy Secretary-General Hecklinger stated that the Roundtable would allow the Guidelines' institutions and the Secretariat to "receive suggestions and a fair evaluation of what can be done to improve outcomes in the supply chain -- what companies can do, what governments should do and what other actors may do as well".

Representatives of the business, labour and NGO communities presented their views to NCPs and discussed some of the implications for supply chain management of this important area of corporate responsibility. Some speakers, participants and adhering governments contributed written material.

The management of the supply chain is relevant for many areas of business ethics covered by the Guidelines -- product safety, environment, technology transfer and labour relations. In the course of the Roundtable discussions, some participants (Steve Canner of the United States Council for International Business, Kristian Ehinger of Volkswagen AG, Maurice Sanciaume of Agilent Technologies and the Australian NCP) noted that supply chain management is a challenge for responsible business across the globe (not just in developing countries) and across the full range of issues covered by the Guidelines. Others emphasised concerns about human rights, working conditions and labour management in supplier sites in the developing world.

The themes of the Roundtable are described below.

Human dimension of the problem

Several participants described, in vivid terms, the difficult conditions under which some people in developing countries work and live. They also noted that some of these conditions are found in the supply chains of OECD-based multinational companies. Neil Kearney (International Textile, Garment and Leather Workers' Federation) cited a study of the results of audits of 300 supplier establishments that was financed and published by a group of leading French retailers. As Mr. Kearney states, "the details make grim reading" -- children under 13 were found working in 2 factories in Bangladesh; non-compliance with minimum wage laws was "common", as were workweeks of "86 hours or more;" auditors also found inadequate occupational health and safety and unsanitary working conditions. Mr. Kearney also noted the "endemic" abuse of workers' rights in Guatemala, including suppliers' recourse to physical force in order to prevent workers from exercising their right to organise. Carol Pier's (Human Rights Watch) study documents obstacles to organising labour unions and the presence of children in the supply chains of major agrifood companies as well as their involvement in dangerous agricultural work in Ecuador's banana sector.

No monopolies on concern about poverty and poor working conditions

Of course, no one in the trade union, NGO or business communities has a monopoly of concern on these issues -- everyone cares about them, but they have different views on how best to improve matters. Participants from the business sector agreed that companies -- through their supply chain management and in other areas -- contribute to the alleviation of poverty, to respecting human rights and to the fair and equitable treatment of workers (Deborah White of Procter and Gamble). They also stated their belief that companies do contribute -- by taking their supply chain responsibilities seriously and via the income generating effects of their trade and investment activities.

André Driessen (Confederation of Netherlands Industries and Employers) underscored the business sector's awareness of the serious problems that supply chains pose for corporate responsibility -- and expressed the business sector's willingness to co-operate with unions, NGOs and host and home governments to search for solutions. Deborah White noted that the solutions to even the relatively narrow and straightforward managerial aspects of this problem are not necessarily simple or obvious, commenting that "we don't have complete answers yet". Ms. White also observed that, in her view, the business community is nevertheless committed to finding answers and encouraging suppliers to observe standards of corporate responsibility like those to which Procter and Gamble subscribe. Recalling points made in the Guidelines commentary and at the OECD Ministerial Meeting 2002, Stephen Canner noted that, while company efforts were generally positive (especially if government policies are well designed), "there are limits to what companies can and cannot do" -- at some points governments have to do their jobs too.

Companies can draw on three sources of principles, standards and norms for behaviour -- domestic law, international declarations and conventions, and private standards

The discussions about principles, norms and behavioural standards noted three sources of guidance for companies -- domestic law, international standards and principles such as the OECD Guidelines, and private norms, such as codes of conduct and other private standards issued by business associations, labour unions and NGOs.

Compliance with law is a core principle of corporate responsibility. Serena Lillywhite (Brotherhood of Saint Laurence) noted that legal standards are not necessarily low in developing countries. She stated that "Chinese labour law sets standards and rules which are as high as those in most OECD countries, although the extent to which they are implemented and influence behaviour in factories varies… the Chinese legal system do[es] not provide strong institutional support for compliance with domestic law. Chinese labour law is complex, made more so by provincial adaptations and exception in special economic zones... The weakness of the Chinese legal institutions means too that workers are reluctant to take steps to secure their legal entitlements, adding to a culture of avoidance of legislated standards." In other words, legal frameworks are sometimes more fully developed than they are commonly given credit for. The challenge is to create the conditions that will motivate a broad set of actors -- civil servants, company managers, workers, civil society -- to push harder to ensure that these legal requirements are respected.

Some participants noted that, in addition to national law, there is a long-standing, widely accepted and evolving framework of principles, standards and conventions. Many of these standards and principles are relevant for companies, as well as for other actors, such as governments. This is particularly true in the field of human rights (e.g. Universal Declaration of Human Rights) and labour rights (e.g. the International Labour Office's Declaration on Fundamental Principles and Rights at Work), where such principles and standards are well established.

Many private standards setting initiatives were referred to in the course of the discussions. These ranged from private codes and associated internal management and reporting programmes (e.g. Deborah White discussed these in the context of Procter and Gamble). The role of industry wide initiatives was also noted (Neil Kearney). The effectiveness of some private certification standards was questioned (see below under "External monitoring and auditing").

How should responsibilities be shared between sourcing and supplying companies?

The sharing of responsibilities between sourcing companies and their suppliers lies at the heart of the challenge of responsible supply chain management. Companies exist as discrete units for reasons of economic efficiency and legal accountability. In order for the concept of "company" to have any legal or economic significance, companies must be defined by legal and operational boundaries. This creates a need for allocation of responsibilities between companies and the other actors with which they conduct business (suppliers, subcontractors, customers, financiers, etc.). The business representatives stressed their view that corporate responsibility in the supply chain couldn't extend to "taking on" other companies' problems -- in particular, not their legal or regulatory responsibilities (André Driessen and Deborah White).

Yet other participants noted that new technologies and management techniques offer companies great flexibility in engineering their operations -- and, by implication, great flexibility in engineering their responsibilities. Jim Baker (International Confederation of Free Trade Unions) noted that the garment and textile sector had already experienced a fundamental restructuring and migration of jobs toward regions with low wages, little respect for worker rights and poor working conditions. Given this scope for engineering the supply chain across legal, regulatory and cultural environments, many of the participants (e.g. Ineke Zeldenrust of the Clean Clothes Campaign) thought that it was unacceptable that companies would then refuse to take responsibility for it. She stressed the importance of understanding the challenge of responsible supply chain management and the need to "break it down … and look at how it can be operationalised." Carol Pier noted that Human Rights Watch's position is that when companies contract directly with supplier, but fail to use their influence those suppliers' respect of labour rights, these companies are complicit in the human rights violations suffered by workers.

Should Small and Medium-Sized Enterprise (SMEs) be held to the same standards?

The participants did not favour the application of a less demanding set of standards and principles to small and medium sized multinational enterprises (e.g. Neil Kearney). Generally, though, it was recognised that SMEs are less aware of the issues and challenges posed by responsible supply chain management. Governments can assist SMEs by helping them to understand the realities of corporate responsibility amongst supply chains in developing countries. This involves understanding the culture, business and legal environment in which they operate, as well as appreciating why worker "empowerment and self-determination" are important (Serena Lillywhite).

SMEs may also face slightly different business situations than those facing large companies (which often have significant leverage over their business partners). For example, Serena Lillywhite noted the importance of "buying organisations" among small companies in the optics industry. Ineke Zeldenrust also noted buying organisations' important role as an intermediary between smaller Dutch importers and world markets. Both viewed promotion of corporate responsibility to these organisations as a potentially promising channel through which corporate responsibility in the supply chain could be encouraged. The point was made that contractual arrangements should include social standards. The Canadian NCP offered the view that the real option of SMEs was to change suppliers if standards were not complied with, from a supplier's perspective the risk of losing customers is important. The delegate from the European Commission drew participants' attention to a new publication focusing on the views of 8,000 SMEs, most of which are "interested and willing to foster corporate responsibility."

Complexity and control

Some participants provided vivid testimony of the complexities of managing the supply chain. Maurice Sanciaume noted the managerial challenges posed by Agilent Technologies' vast supply chain where the company acts as both a purchaser and a supplier. Deborah White noted that Procter and Gamble has 106,000 employees in 80 countries. These work to provide 250 consumer brands to five million consumers located in more than 130 countries. The company has over 100,000 suppliers and the nature of the contractual relations with these suppliers varies from "arms length" spot-like transactions to closely managed relations with what the company calls "mission critical" suppliers. All agreed that the control problems in the supply chain are influenced by sectoral considerations.

Serena Lillywhite stated, in connection with the outsourcing relations that she has looked at in China, that "it is important to recognise that corporate responsibility amongst supply chains is a very complex issue. The conceptual and ethical task of dealing with Chinese factories is difficult for the small firm, even one committed to doing everything possible to operate in an ethical manner. It requires time, resources and commitment. Specialist staff are needed with expertise and knowledge of the labour and environmental issues, and regulatory environment of developing countries."

"No excuses -- engineer processes so that basic labour rights can be respected"

Several participants warned against using complexity as an excuse for not taking responsibility (Neil Kearney, Ineke Zeldenrust, Jim Baker). Companies readily accept responsibility for product quality in the supply chain. They engineer their supply chain management practices to ensure acceptable standards of product quality. Some participants felt that, if they can do it in this area, they should be able to adopt similar control mechanisms for other aspects of corporate responsibility, such as respecting core labour rights.

Ineke Zeldenrust emphasised the power and leverage that stem from longer-term supplier relations and urged companies to favour such relations. She also called for elimination of the separation of corporate responsibility and sourcing functions because the design of sourcing systems needs to "incorporate fully corporate responsibility considerations."

Deborah White felt that, while it has some merit, this argument about re-engineering supply chains can be exaggerated. She noted in particular the legal concerns that might arise. Doug Worth (Business and Industry Advisory Committee) asked Roundtable participants not to neglect what can be high costs of extensive restructuring of contractual relationships. He noted his own experience in the computer industry shows that a change of major suppliers could cost a company up to a billion dollars. In contrast, Neil Kearney said that his experience shows that such restructuring can be accomplished at relatively little cost in some sectors. Kristian Ehinger, cited Volkswagen's experiences in China (see below) as an example where government policies -- notably those influencing management and control -- can have an effect on companies' abilities to influence supplier conduct.

Internal controls

Supply chains are one of the major challenges of risk management. André Driessen noted that "things will inevitably go wrong in complex supply chains -- companies need to have the ability to deal with problems once they are identified". There is also a need to develop the ability to adopt measures to prevent reoccurrence of problems. However, there will be differences in the nature of the problems and appropriate management tools among companies and across different sectors and countries.

Deborah White provided an example of the internal controls used by Procter and Gamble to monitor relations with its 100,000 suppliers. The company separates suppliers into raw material suppliers and contract manufacturers. It has a global purchasing organisation that assures that products are safe for consumers and for workers. However, its personnel are not trained to monitor for other aspects of corporate responsibility, such as respect for human rights. In terms of broader measures, it has sent 10,000 "mission critical" suppliers a booklet containing corporate responsibility guidelines. It has also modified contract language to require compliance with local labour law. The company also has programmes for corrective action and internal monitoring, and uses threats of terminating relationship as another source of leverage.

Kristian Ehinger advised participants not to neglect the importance of internal measures, such as those used by Procter and Gamble. In his view, these efforts to promote responsible supply chain management are likely to be more effective -- in terms of both performance and cost -- than external measures.

External monitoring and auditing

This year's focus on the supply chain extended a theme that was already developed at last year's Roundtable. Both discussions cautioned against exaggerating the contributions that external audits and monitoring can make to resolving supply chain issues. The limits of these tools involve both their costs and effectiveness.

The business community emphasised the sometimes-prohibitive costs of external monitoring and audits. Deborah White's reference to her company's 100,000 suppliers vividly illustrates how large a task conducting external monitoring of all suppliers can be. BIAC's written contribution states: "It is not economically or logistically feasible for all enterprises to monitor and audit all their suppliers. The best way to monitor and audit the social and environmental performance of all firms is for national governments to implement and enforce national laws and regulations that protect workers and the environment."

Other participants questioned the effectiveness of external monitoring and audits. Roy Jones (Trade Union Advisory Committee; TUAC) asked the basic institutional question -- "who is auditing the auditors?" He highlighted the importance of sustainability and self-determination through education and training. In the absence of widely agreed performance, audit and reporting standards, it is not surprising that the social audit industry sometimes produces reports that are of doubtful accuracy and completeness. Carol Pier noted, in particular, that one of the companies in her study was a "signatory member" of a prominent social audit and certification scheme that is designed to check for adherence to appropriate social standards in the supply chain. According to her study's allegations, the company's suppliers in Ecuador employ children in dangerous operations and make it difficult to organise labour unions, but these labour rights abuses do not violate the terms of the companies' membership in the audit and certification scheme.

Workers' rights -- a decentralised mechanism for monitoring and accountability

Other participants questioned the feasibility of using both external auditing and internal controls to monitor performance at millions of production sites spread across the globe. Jim Baker emphasised the role of rights -- especially labour rights -- in facilitating decentralised monitoring of corporate performance. One cannot "pretend that people can be protected by remote control". He stated that no matter what kind of system of internal or external control a company might adopt, it is going to "come up wanting" relative to a system where workers can protect their own rights.

Serena Lillywhite developed a similar theme, noting the relationship between workers rights and the effectiveness of the legal and regulatory environment in China. She discussed the deficiencies not just of formal enforcement, but of other more decentralised processes, such as workers' abilities to act on their own to "secure their legal entitlements without fear of reprisal". Her experiences in China suggest that codes of corporate conduct, alone, cannot guarantee protection of workers' rights.

The Netherlands NCP noted that he had been asked to consider a specific instance in relation to the outsourcing activities of a small Dutch company in India. He wondered whether he should view the two core labour standards brought up by the specific instance -- child labour and freedom of association -- as being of equal importance.

The NGO and trade union communities rejected the notion that some labour standards are more important than others.

Government role

As was the case with last year's Roundtable, this year's participants all agreed that governments need to assume their rightful roles as regulators and legal enforcers. For example, BIAC's written contribution states: "Government implementation and enforcement of national laws and regulations are essential for creating competitive markets, protecting the environment and safeguarding individual rights…. [I]n some countries a lack of resources and an inadequate institutional infrastructure inhibits the ability of countries to effectively enforce these laws. The only long term solution to such failures is for government to create an enabling environment for investment-led domestic growth that will create the resource base necessary to implement and enforce the law on all companies, regardless of size or nationality of ownership".

But some Roundtable participants emphasised that lack of government responsibility is not an excuse for lack of corporate responsibility. Neil Kearney said " the corporate world must, even in the absence of regulation or its implementation, respect international norms voluntarily." Ineke Zeldenrust pointed out that companies are not passive victims or poor regulatory environments -- they can choose where they invest and where they out-source.

BIAC's written contribution to the Roundtable notes the limits of substituting a corporate role for government roles via supply chain management. The chief limitation "may be [the supply chain's] inability to reach the vast majority of people in the world who produce goods for local consumption or work outside the formal economy. For these people attempts to enforce local law through the global supply chain would bring little or no benefit." In other words, world poverty is a pressing problem -- but the supply chain is only one piece in the larger puzzle of economic development.

Responsible business -- cost or competitive advantage?

The question of whether responsible supply chain management is a cost or a competitive advantage for sourcing and supplying companies is important for many aspects of the supply chain debate. For example, if responsible management is profitable, then "selling" responsibility in this field may involve no more than raising awareness and highlighting best practice. In some sense, if responsible management is a profit centre, then good corporate citizenship becomes a self-enforcing proposition. On the other hand, if responsible conduct is costly to companies or if it creates winners and losers in the broader economy, then the issues of creating norms for business conduct and incentives for respecting them assume greater importance.

The Roundtable discussions were, not surprisingly, unable to resolve this basic quandary. Examples and experience were described that pointed in both directions. Neil Kearney related experience that suggested that responsible management is an investment, not a cost. He described his knowledge of supplier operations in a region of India where there was "massive child labour and abuses of workers' rights and horrendous working conditions". Improvements to working conditions not only made workers "better off, but the supplier company says that it has seen improved productivity, improved product quality and higher profitability. Serena Lillywhite's intervention also suggested that some Chinese entrepreneurs are interested in creating "ethical production" as a source of competitive advantage, but this of course would require some way of demonstrating that such suppliers are indeed "ethical".

On the other hand, other interventions suggested that responsible management could be very costly. These include the costs of actually raising the standards (e.g. managing product demand so as to not create crushing work loads for suppliers' workers; paying for more social services) and the costs of monitoring production sites and communicating performance to the broader world. The business community noted that these costs could range from modest to astronomical depending on the nature of the problem and the sector.

Transparency

There was widespread agreement among Roundtable participants on the importance of transparency. All felt that enhanced transparency would help create the conditions that would promote responsible supply chain management. However, there was less agreement on the scope or means of promoting transparency.

Many of the NGO and trade union participants called for "full disclosure in the supply chain" -- this refers to extensive publication of the names and locations of suppliers. While most speakers referred to voluntary initiatives in this area, Serena Lillywhite and Neil Kearney thought that a government requirement that the label "country of origin" be put on certain products would be a useful step toward greater transparency. By way of example, Serena Lillywhite cited the complex licensing arrangements that allow some brand name optical frames to be labelled as "Made in Italy" when, in fact, 75 percent of production occurs in China.

However, some business representatives felt that full disclosure would force companies to reveal business secrets. Doug Worth and Kristian Ehinger both stressed that, at least in the computer and automotive industries, supply chain practices embodied business secrets. Any attempts to enhance transparency would have to somehow safeguard these secrets.

In contrast, Serena Lillywhite's experience in the optics industry showed that, at least in that sector, competitors routinely visit supplier sites. She found little problem there of revelation of business secrets, though she noted that factory visits were sometimes used as a means of gathering information about their competitors' designs. Deborah White noted that Procter and Gamble sees itself as a leader in this area; it believes strongly in transparency and engages in extensive reporting.

Development impacts

Overall, the assessment of the development impacts of supply chain activity was positive. Steve Canner asked: "Does responsible supply chain management matter for producers, workers and developing countries? Are the Guidelines a source of hidden protectionism or a source of competitive advantage in the global marketplace?" He provided answers at the aggregate level -- at the level of overall economies. He noted that the aggregate answer depends on the interlocking "policy mosaics" of countries and of companies. If these two groups of actors manage to work well together, then supply chain activities can bring major benefits to producing countries -- in terms of environmental protection, human capital accumulation and technology transfer. He cited the OECD's study "Foreign Direct Investment -- Maximising Benefits, Minimising Costs" as supporting the view that, if the "enabling environment" is well designed, then the benefits of hosting multinational enterprises (including sourcing activities) are also positive.

Kristian Ehinger noted that Volkswagen is obliged to enter into 50-50 joint venture arrangements in China due to local control requirements. He notes that these requirements, combined with local content requirements, make it difficult for Volkswagen to manage this company the way it would like. It is nevertheless making an effort. It has signed a company framework agreement -- a private contract signed with international labour federations -- with regard to core labour standards that will apply to China's environment. He also notes that Volkswagen's suppliers -- which have followed it into the Chinese market -- bring technology and other know-how with them. This is a major development benefit for China.

The Brazilian delegate noted that these efforts help to build institutional and legal capacity. In Brazil, they create a benchmark that everyone can use to understand responsible management. This is an "ongoing, maturing process". He cited, as an example, the concept of sustainable development. While at one time it was not well known or accepted, it has become a useful, mainstream concept that everyone -- companies, trade unions, civil society and governments -- can use to discuss and understand a range of issues for government and corporate policy.

Moving toward a common view -- The contribution of the Guidelines

Roundtable participants largely agreed that, in the long run, a durable solution to supply chain problems depends on establishing appropriate frameworks of rules and regulations. They also seemed to agree that such frameworks are currently deficient in some countries. Neil Kearney favoured a combination of "regulation, global and national, and voluntary effort" in order to improve these frameworks. BIACs conclusions -- entitled "The Way Forward" -- point in this same general direction; they state that "Business generally agrees that the best way to promote improved labour and environmental standards in a direct supplier or subcontractor is to convince them that it is in their interest to improve standards and conditions…" and that voluntary initiatives should not "divert attention from the primary means for promoting environmental and social protections: the implementation and enforcement of national laws and regulations".

However, despite this broad agreement on the importance of appropriate law and regulation, there were major differences of view on the nature and extent of corporate responsibility when companies operate in environments where legal and regulatory frameworks are not functioning well. Roundtable participants expressed a variety of views in most of the areas reviewed above -- on the nature and extent of responsibility in the supply chain, on the degree to which companies can be expected to alter their investment decisions and internal management practices in order to respect norms for responsible behaviour. However, many participants pointed to the extensive body of international declarations, conventions and instruments -- including the OECD Guidelines -- that companies can draw on when formulating their policies and management practices.

The contribution that the Guidelines can make to improving supply chain practices is linked, according to some participants, to the overall effectiveness of the Guidelines and their implementation mechanisms. Carol Pier posed a number of challenges for improving the effectiveness and "functional equivalence" of NCPs (for example, she asks how NCPs decide whether a specific instance "merits further examination" and whether the relevant actors are sufficiently aware of them in particular national contexts). Serena Lillywhite urged greater "consistency of export-import credits and other government policies with the Guidelines". The issue of whether the Guidelines apply only to trade or to both trade and investment was a subject of debate. Patricia Feeney (Rights and Accountability in Development) and Roy Jones stated their view that the Guidelines apply to both. The business community stated its view that, since the Guidelines are part of the Declaration on International Investment and Multinational Enterprises, they only apply to international investment. The comments of several NCPs also suggested that there might be a need for further reflection and consideration of this issue.