



RSC 2023/28  
Robert Schuman Centre for Advanced Studies  
Global Governance Programme

# WORKING PAPER

**The Potential of Contractual Assurances to  
Advance Supply Chain Due Diligence**

Jaap Baaij and Alex Geert Castermans

European University Institute  
**Robert Schuman Centre for Advanced Studies**  
Global Governance Programme

## **The Potential of Contractual Assurances to Advance Supply Chain Due Diligence**

Jaap Baaij and Alex Geert Castermans

RSC Working Paper 2023/28

This work is licensed under the [Creative Commons Attribution 4.0 \(CC-BY 4.0\) International license](https://creativecommons.org/licenses/by/4.0/) which governs the terms of access and reuse for this work.

If cited or quoted, reference should be made to the full name of the author(s), editor(s), the title, the series and number, the year and the publisher.

ISSN 1028-3625

© Jaap Baaij & Alex Geert Castermans, 2023

Published in March 2023 by the European University Institute.  
Badia Fiesolana, via dei Roccettini 9  
I – 50014 San Domenico di Fiesole (FI)

Italy

Views expressed in this publication reflect the opinion of individual author(s) and not those of the European University Institute.

This publication is available in Open Access in Cadmus, the EUI Research Repository:

<https://cadmus.eui.eu>

[www.eui.eu](http://www.eui.eu)



With the support of the  
Erasmus+ Programme  
of the European Union

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

### **Robert Schuman Centre for Advanced Studies**

The Robert Schuman Centre for Advanced Studies, created in 1992 and currently directed by Professor Erik Jones, aims to develop inter-disciplinary and comparative research on the major issues facing the process of European integration, European societies and Europe's place in 21st century global politics.

The Centre is home to a large post-doctoral programme and hosts major research programmes, projects and data sets, in addition to a range of working groups and ad hoc initiatives. The research agenda is organised around a set of core themes and is continuously evolving, reflecting the changing agenda of European integration, the expanding membership of the European Union, developments in Europe's neighbourhood and the wider world.

For more information: <http://eui.eu/rscas>

The EUI and the RSC are not responsible for the opinion expressed by the author(s).

### **The Global Governance Programme**

The Global Governance Programme is one of the flagship programmes of the Robert Schuman Centre. It is a community of outstanding professors and scholars, that produces high quality research and engages with the world of practice through policy dialogue. Established and early-career scholars work on issues of global governance within and beyond academia, focusing on four broad and interdisciplinary areas: Global Economics, Europe in the World, Cultural Pluralism and Global Citizenship.

The Programme also aims to contribute to the fostering of present and future generations of policy and decision makers through its executive training programme: the Academy of Global Governance, where theory and 'real world' experience meet and where leading academics, top-level officials, heads of international organisations and senior executives discuss on topical issues relating to global governance.

For more information: <http://globalgovernanceprogramme.eui.eu>

## **Abstract**

On February 23, 2022, the European Commission's adopted a proposal for a Directive on corporate sustainability due diligence. The proposed Directive requires companies to make their supply chains sustainable by obtaining contractual assurances from their suppliers. Noncompliance is met with administrative sanctions and civil liability. In this contribution, we question the ability of contractual assurances to sufficiently influence business conduct in the supply chain. Imposing sanctions and civil liability do not resolve the difficulties that may, in practice, impede the control of supply chains through contracts. Therefore, based on recent empirical research and existing general conditions used by twelve multinational companies, we offer recommendations that can help companies manage their supply chains contractually and thus contribute to the effectiveness of the proposed Directive.

## **Keywords**

Legal accountability; Contract Law; Corporate sustainability; European law; Supply Chain

## Table of contents

1. Introduction	7
2. The heart of the proposed Directive: contractual assurances and a monitoring procedure	8
3. Questioning the effectiveness of the proposed Directive	10
3.1. The Directive's Duty-Imposing Nature	10
3.2. A Distorted Image of the Supply Chain	11
4. Purchase and sales terms and conditions in practice	13
4.1. Introduction	13
4.2. The extent of sustainability obligations	14
4.3. Influence on admission and expulsion of chain participants	15
4.4. The content and scope of commitments to sustainability	15
4.5. Deployment of the termination power	18
4.6. A balanced monitor mechanism	20
4.7. The importance of cooperation	22
5. Conclusion	23
List of procurement terms and conditions and Supplier Codes of Conduct consulted	24

# 1. Introduction

On February 23, 2022, the European Commission adopted a proposal for a directive on corporate sustainability due diligence in the field of the environment and human rights.<sup>1</sup> The proposed Directive provides a horizontal framework applicable to - in short - large companies located (Art. 2(1)) or operating (Art. 2(2)) within the European Union, regardless of the economic sector. These enterprises are obliged to identify (Art. 6), prevent (Art. 7), and eliminate or minimize (Art. 8) actual and potential negative effects on human rights and the environment (Art. 4(1) exordium). Here, the Directive does not only cover the effects of the company's or of its subsidiaries' activities but also those of established business partners in its chains of activities (Art. 1 para. 1 sub a).<sup>2</sup> Due diligence is therefore not limited to the business operations of merely the companies with which the company has a direct, contractual relationship (so-called "tier 1" suppliers) but also extends to those of the lower-tier suppliers ("tier 2," "tier 3," and so on), provided the relationship can be considered "established."

The primary goal of the proposed Directive is to contribute to realizing the European sustainability goals as articulated in the "European Green Deal" following the 2015 Paris Climate Agreement and to protecting human rights.<sup>3</sup> The secondary goal, i.e., the means of shaping the primary goal, is improving the sustainability of, among other things, global supply chains of companies based or operating within the European Union. Finally, the tertiary goal, which serves to realize the secondary goal, is for companies to obtain contractual assurances from direct and indirect business partners in the supply chain to comply with codes of conduct.

The proposed Directive employs the rules of private law rules instrumentally. On the one hand, the Directive treats commercial contracts not as a tool for companies to shape their legal relationships freely but as the way in which companies are to comply with the Directive's rules. Indeed, the proposal relies heavily on the use of commercial contracts as an instrument by which the company is to exercise control over activities in the supply chain.

On the other hand, the Directive uses tort law not primarily to provide injured parties with a remedy but as a penalty to force companies to comply with the prescribed use of contracts. Indeed, the Directive creates a two-pronged penalty system to induce companies to take the necessary action. If a company fails to exercise due diligence, it will not only be punished with "effective, proportionate, and dissuasive" sanctions (Art. 20(1)) such as monetary fines (Art. 20(3)).<sup>4</sup> National laws should also make it possible that the company is subject to civil liability for damages caused by violation of the national implementation of the Directive (Art. 22). At the national level, these sanctions will likely result in administrative enforcement, respectively tortious liability.<sup>5</sup>

In this contribution, we question this instrumental use of private law, not from a legal-political perspective<sup>6</sup> but from the viewpoint of effectiveness. It is likely that making supply chains more sustainable will contribute to achieving the primary objective of the proposed Directive to combat climate change. The Commission observes that 80-90% of the environmental damage caused by

---

1 Proposal for a Directive on due diligence in corporate sustainability and amending Directive (EU) 2019/1937 (2022/0051 (COD)), <https://eur-lex.europa.eu/legal-content/NL/TXT/?uri=CELEX:52022PC0071>; a revised proposal has been published on 22 November 2022.

2 Business chain means the activities associated with the production of goods or the provision of services in the broad sense of the word (art. 3 sub f). It refers to the activities of business partners with whom the company has a so-called "established business relationship" (art. 1 sub a), that is, a direct or indirect business relationship that can be considered sustainable in terms of its intensity or duration, and, moreover, is not merely a negligible or incidental link in the chain (art. 3 sub f).

3 Recitals 1 to 13 of the preamble.

4 See recital 54 of the preamble.

5 See, for example, in the Netherlands, EK 2021–2022, 22 112, IS (Letter from the minister of foreign affairs), p. 3, 12. TK 2021–2022, 22 112, nr. 3429 (Report of a written consultation), p. 23, 28.

6 The pertinent legal-political questions raised by the European Commission's proposed directive concern, among other things, the conditions under which companies have a social responsibility for the management of companies in their supply chain, and to what extent government intervention is legitimized or in line with the freedom of enterprise enshrined in Article 16 of the EU Charter of Fundamental Rights. We leave the answers to such questions for another time.

European production results from supply chains located outside the European Union.<sup>7</sup> Studies in the last decade confirm this statement, showing that, globally, the majority of greenhouse gas emissions do not result from the business processes of companies themselves but from the companies in their supply chains.<sup>8</sup> Whether making global supply chains more sustainable will come in time to meet the Climate Targets by 2030 is not certain. Still, a positive adjustment in the activities of supply chains will contribute to lessening the burden on the environment is to be expected.

However, we question the Directive's reliance on companies' ability to control supply chain activities through commercial contracts. Here we are not referring to whether the proposed Directive will be able to incentivize companies to obtain contractual assurances from their suppliers sufficiently but whether these assurances will, in reality, improve supply chain activities. After all, the supply chain must, in reality, be rid of forced labor, child labor, discrimination, environmental pollution, and biodiversity degradation.

Article 12 of the proposed Directive requires the European Commission to adopt guidelines for non-binding model contractual clauses to help companies meet the obligations of Articles 7 and 8.<sup>9</sup> In this contribution, we offer some preliminary suggestions for the implementation of these guidelines and, thus, for increasing the effectiveness of contractual assurances and perpetual clauses. To this end, we will first elaborate on the key role that the proposed Directive attributes to contractual assurances that companies must obtain from their supply chains (par. 2). We then argue why the effectiveness of the Directive's rules is problematic and why it is necessary, therefore, to gain insights from the practice of supply chains (par. 3). Finally, based on real-life examples of procurement and sales contracts and recent empirical studies of supply chain management, we present several recommendations for the guidelines that are to assist companies in drafting and managing contracts in their supply chains (par. 4).

## 2. The heart of the proposed Directive: contractual assurances and a monitoring procedure

How does the proposed Directive propose companies prevent and reduce the negative impact of their activities? Article 7 answers this question for situations with *potential* negative impacts, while Article 8 does the same for when the negative impact has already occurred. Given the fact that the language of these articles is nearly identical, we focus on Article 7 to avoid unnecessary repetition.

According to Art. 7(2)(a) if the Directive, companies are first to draw up and implement an "action plan." This article limits this obligation to cases where "where necessary due to the nature or complexity of the measures required for prevention." For the everyday practice of the kind of large companies targeted by the Directive, this will mean that while every company will need to develop an action plan, it is not required to identify and address every possible risk associated with its business activities. Apparently, the code of conduct may be considered sufficient guidance for some measures.

Subsequent provisions show the role that the Directive sees for contract law. According to Art. 7(2) (b):

"Companies shall be required to ... seek contractual assurances from a business partner with whom it has a direct business relationship that it will ensure compliance with the company's code of conduct and, as necessary, a prevention action plan, including by seeking corresponding contractual assurances from its partners, to the extent that their activities are part of the company's chain of activities (contractual cascading) ..."<sup>10</sup>

7 Explanation to the Proposal, p. 9.

8 E.L. Plambeck, 'Reducing greenhouse gas emissions through operations and supply chain management,' *Energy Economics* 34 (2012) S64–S74, p. S65; CDP, 'Transparency to Transformation: A Chain Reaction. CDP Global Supply Chain Report 2020', 2021, p. 5. CDP.net/en/research/global-reports/transparency-to-transformation; A.-T. Bové & S. Swartz, 'Starting at the Source: Sustainability in Supply Chains', McKinsey&Company 2016, , p. 3, <https://www.mckinsey.com/capabilities/sustainability/our-insights/starting-at-the-source-sustainability-in-supply-chains>

9 The English language version of Article 12 speaks of "guidance about voluntary model contractual clauses". See also preamble, recital 45.

10 Compare Art. 8(3)(b) for the case in which the negative effects have since occurred and the company is required to undo or mitigate the negative effects; this is a corrective action plan.



This provision raises two questions of interpretation.

First, the proposal does not define or clarify the form of ‘contractual assurances.’ In the language of common law contracts, contractual assurances have a broad meaning that includes promises such as covenants, conditions, representations, and warranties.<sup>11</sup> However, legislative proposals adopted by the Commission exist in 24 language versions.<sup>12</sup> As English, German, and French are the European Commission’s procedural languages,<sup>13</sup> it is remarkable that the German and French language versions of the Directive appear to offer a more restrictive interpretation than the English one. While the words ‘*Zusicherungen*’ in the German version translates as ‘assurances,’ the English equivalent of the word ‘*garanties*’ in the French version and ‘*garanties*’ in the Dutch version would be ‘warranties.’ Notwithstanding these variances, the broader English concept is likely the most reliable. In the European legislative process as well as the interpretation of European law, the English version of EU legislative texts carries de facto more weight than other versions.<sup>14</sup> Therefore, assurances, as used in Art. 7(2)(b) is likely to be interpreted extensively. At least for now, the European Parliament and the European Council will adopt the final wording of the 24 language versions of the final legislative act if the Commission’s proposal is adopted.

The second interpretation question what kind of obligation the Directive envisions when it obliges companies to seek contractual assurances from their suppliers raises the question That a company must “seek” to obtain contractual assurances from its business partners indicates that this provision does not appear to impose on the company an obligation of result. For this reason, the company which, despite frantic efforts, fails to obtain an assurance as referred to here in the contract will likely not be held liable under Article 22.

On the other hand, if a company fails to obtain assurances, it does not mean it can simply continue working with the same business partner. It will have to examine whether the negative consequences, which are now not covered by the contract, can be avoided by other means by concluding a contract with other parties (Art. 7(3)).<sup>15</sup> The Directive refers to an “indirect partner,” a company lower or higher in the business chain. Art. 7(5)) stipulates that if these latter contracts do not provide sufficient relief or if the reality develops in a negative direction despite the assurances, the company may have to refrain from further cooperation with the business partner:

“As regards potential adverse impacts within the meaning of paragraph 1 that could not be prevented or adequately mitigated by the measures in paragraphs 2, 3 and 4, the company shall be required to refrain from entering into new or extending existing relations with the partner in connection with or in the chain of activities of which the impact has arisen and shall, where the law governing their relations so entitles them to, take the following actions:

... (b) terminate the business relationship with respect to the activities concerned if the potential adverse impact is severe.

Member States shall provide for the availability of an option to terminate the business relationship in contracts governed by their laws.”<sup>16</sup>

Hence, the fruitless fulfillment of the best-efforts obligation can thus turn into an obligation of result: the non-contraction or termination of the legal relationship with the business partner. Still, according to Recital 36 of the preamble, the Directive views legal relationship termination as a last resort:

11 See, e.g., Barry Fink, Contractual Assurances in Multinational Agreements to Purchase or Sell U.S. Businesses--Cultural Differences Heighten Normal Conflicts, 14 Hastings Int'l & Comp. L. Rev. 387, 388 (1991).

12 Available in Eur-lex, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52022PC0071>.

13 See Court of Auditors, Special Report (No 9/ 2006), C284/ 8.

14 On this subject, see Chapter 3 of C.J.W. Baaij, *Legal Integration and Language Diversity: Rethinking Translation in EU Lawmaking*, Oxford University Press: 2018.

15 Compare Art. 8 lid 4.

16 Compare art. 8 lid 6.

“In order to ensure that prevention and mitigation of potential adverse impacts is effective, companies should prioritize engagement with business relationships in the chain of activities, instead of terminating the business relationship, as a last resort action after attempting at preventing and mitigating adverse potential impacts without success.”

Any need to terminate a legal relationship with the business partner is therefore preceded by a temporary “suspension.” During the suspension, the business must continue to prevent and minimize the negative effects of the impacts if such efforts are reasonably expected to succeed in the short term (Art. 7(5)).

The obligation to obtain contractual assurances does not stand on its own. Such assurances are nothing more than empty words if the contracting parties do not follow up. Therefore, in Article 7, the Directive gives several instructions about the monitoring of compliance with the assurances.

First, appropriate measures must also be taken to monitor compliance with the contractual commitments, code of conduct, and action plan (Art. 7(4)). The provision adds that fair, reasonable, and non-discriminatory terms must be used in the legal relationship with small and medium-sized enterprise partners. If this involves using an independent third party, the company shall bear the cost of the verification by an independent third party. Conditions should be prevented from being pushed through without regard to their financial and economic impact on the other party or subsequent parties in the supply chain.

Second, companies should provide targeted and proportionate support to their SME business partners with whom they have an established business relationship if compliance with the Code of Conduct or the Preventive Action Plan would jeopardize the viability of the business partner (Art. 7(2) (d)). Recital 34 of the preamble offers illustrations of the nature of such support:

“... financing, for example, through direct financing, low-interest loans, guarantees of continued sourcing, and assistance in securing financing, to help implement the code of conduct or prevention action plan, or technical guidance such as in the form of training, management systems upgrading.”

Notwithstanding the proposed Directive’s attempt to make the contractual assurances effective, next, we explain why we question the instrument’s efficacy.

### **3. Questioning the effectiveness of the proposed Directive**

#### **3.1. The Directive’s Duty-Imposing Nature**

The proposed Directive’s instrumental use of private law potentially hinders its effectiveness.

General private law facilitates trade with rules of supplementary law.<sup>17</sup> Legal rules that allow private actors to create legally enforceable rights and obligations through contracts can be considered “power-conferring” rules.<sup>18</sup> In contrast, the proposed Directive uses contracts as part of “duty-imposing” rules. Articles 7 and 8 do not present contractual assurances and cascading obligations, nor their adequate enforcement, as a form of empowerment but as an obligation. Here, the administrative sanctions of Article 20 present a penalty for noncompliance with this obligation.

The prospect of civil liability regulated by Article 22 also reflects the duty-imposing nature of the rules on contractual assurances. To be precise, the rule of Article 22 has both a duty-imposing and a power-conferring side. On the one hand, the provision testifies to a duty-imposing rule insofar as the company must comply with the duty of care on pain of liability for compensation for damages

<sup>17</sup> See, for example, Asser/Sieburgh 6-III 2018, nrs. 41 en 378.

<sup>18</sup> Here we refer to the well-known distinction between so-called ‘duty-imposing rules’ and ‘power-conferring rules’ that we find in Hart, H.L.A., *The Concept of Law* (3d ed. 1961/2012), p. 27-28, 81.

resulting from a violation.<sup>19</sup> On the other hand, Art. 22, as an instrument of private law enforcement, also has a power-conferring component. After all, it empowers the alleged victim to invoke a remedy, if desired, by, for example, bringing an action for damages in tort. Still, Article 22 is best qualified as primarily a duty-imposing rule. The second paragraph of Article 22 underscores that civil liability serves primarily as a sanction by providing that a company may not be held liable for damages if it has obtained and enforced the contractual assurances. Moreover, nowhere does the proposed Directive give any attention to the victims of the adverse effects of supply chains, for example, to explain how they could enforce their rights.

In two respects, the duty-imposing nature of the proposed Directive described here may get in the way of effectively making supply chains more sustainable and thus achieving European sustainability goals.

First, duty-imposing rules are backward-looking: administrative sanctions and civil liability are primarily concerned with penalizing misdeeds already committed or the compensation of damages already incurred. The retroactive nature of duty-imposing rules makes the Directive's provisions on contractual assurances a bad fit for its purpose. After all, the Directive is forward-looking as it seeks to prevent or at least reduce environmental damage and human rights violations.

Of course, ex post retaliation and compensation can have an ex ante deterring effect, thus preventing undesirable behavior and its harmful effects. Concerning administrative sanctions, Article 20 even explicitly states that these must have a "dissuasive" effect. However, that effect does not necessarily lead to the desired results. Insofar fines and an obligation to pay damages indeed deter companies from undesirable behavior, they do so by making that behavior more expensive and, thus, less appealing. Hence, sanctions do not facilitate or expedite the desired behavior. Put differently, fines and damages do not necessarily make the sustainability of supply chains easier or cheaper.

This observation brings us to the second objection to the duty-imposing nature of the proposed Directive's provisions: requiring companies to include contractual assurances and cascading obligations in their contracts and to enforce them does not, in and of itself, make the desired sustainability of supply chains a reality. Even if the sanctions of Articles 20 and 22 will move every company to comply with the due diligence obligation, they will not necessarily remove the practical obstacles that may, in reality, prevent the successful influence of the supply chain through contracts.

Thus, as far as we are concerned, the effectiveness of the Directive proposed by the Commission will have to depend not on the deterring effect of the proposed sanctions but on the effectiveness of the contractual clauses that companies will formulate and the monitoring of their compliance. The question that must be answered, therefore, is whether these clauses are capable of steering the behavior of established relationships in the supply chain.

### **3.2. A Distorted Image of the Supply Chain**

The effectiveness of the proposed Directive is also problematic with respect to the underlying understanding of the nature of supply chains. The Commission's decision to make companies responsible for the activities of its direct and indirect business partners shows that the Commission assumes a hierarchical supply chain model. In that depiction, the company acts as a quasi-legislator of the chain through commercial contracts, its code of conduct, and an action plan.<sup>20</sup> Market power in this model is concentrated exclusively or primarily at the level of the company – or: the focal,<sup>21</sup> lead,<sup>22</sup>

19 H.L.A. Hart considered the nature of liability law as obligation-imposing, see John C.P. Goldberg & Benjamin C. Zipursky, *Seeing Tort Law From the Internal Point of View: Holmes and Hart on Legal Duties*, 75 *Fordham L. Rev.* (2006), p. 1575.

20 For the description of such a "command and control" model of trade chains, see, F. Cafaggi, 'Regulation through contracts: Supply-chain contracting and sustainability standards', *ERCL* 2016/12, afl. 3, p. 223.

21 See Christopher, M., 1992. *Logistics and Supply Chain Management*. Pitman, London.

22 See, e.g., S. Laari et al., 'Leveraging supply chain networks for sustainability beyond corporate boundaries: Explorative structural network analysis,' *Journal of Cleaner Production* 377 (2022) 134475.

or buying firm.<sup>23</sup> Here, the company is, in essence, the ‘chain leader.’<sup>24</sup> Indeed, firms producing consumer goods tend to have relative market power vis-à-vis their suppliers and thus a position from which to influence the supply chain.<sup>25</sup> In this context, the use of contracts represents a potentially effective means of controlling the sustainability of supply chains.

However, the reality may also be quite different. First, rather than a hierarchical, linear concatenation of enterprises, in reality, supply chains resemble more ‘webs’<sup>26</sup> or ‘networks’<sup>27</sup> of suppliers. Suppliers usually do not have a single but multiple customers or buyers, which often operate in the same market as competitors. So it happens that different companies make use of the same direct and indirect suppliers.<sup>28</sup> In other words, supply chains overlap and are integrated vertically and horizontally.

Second, when the Directive speaks of direct and indirect business relationships, it suggests that supply networks are transparent and its participants discernible. The reality is that, over the years, global supply chains have grown larger and more complex, now sometimes consisting of thousands of producers spread across the globe.<sup>29</sup> Being able to map and visualize one’s supply chain is critical for a company to monitor processes and improve its supply chain’s sustainability.<sup>30</sup> Yet, mapping entire supply chains and tracing each participant has indeed proven to be one of the biggest real-life challenges in supply chain management.<sup>31</sup>

Third, even if lower-tier suppliers are visible to the focal firm, they will be further removed from the company’s direct control.<sup>32</sup> The proposed Directive presumes companies have the capability to control their supply chain by leveraging their market power against their direct suppliers and indirectly against the lower-tier suppliers. The reality is that a company’s influence on a web of suppliers might be less than significant. For example, its power will be diminished when a chain participant is not dependent on this company’s business. This is the case, for example, when a supplier with multiple customers may not be reliant on any of its customers, especially when a customer only represents a small portion of a supplier’s overall business.<sup>33</sup> Furthermore, a supplier is less subjected to a buyer’s influence when the supplier faces little competition or has a monopoly position.<sup>34</sup> In these situations, a supplier may have little incentive to adhere to one of its customer’s contractual CSR obligations,<sup>35</sup> at least when adhering to these stricter obligations involves relatively high costs.

The reality of a global supply chain detracts from the potential of a company’s use of contracts to steer behavior in its supply chain. It does not support the Directive’s approach of designating individual companies as the focal point of responsibility. In its explanatory statement for the proposed Directive, the Commission does, to some extent, acknowledge the complexity of supply chains, the lack of sufficient information, and the cost of taking responsibility for the negative impacts of their

23 See, e.g., M. Jia et al., ‘A systematic literature review on sustainability-oriented supplier development,’ *Production Planning & Control* (2021).

24 Cafaggi 2016, p. 230.

25 Bové & Swartz 2016, p. 6.

26 Cafaggi 2016, p. 225.

27 Villena 2018, 66.

28 Zie Cafaggi 2016, p. 241.

29 M.M. Wilhelm et al., ‘Sustainability in multi-tier supply chains: Understanding the double agency role of the first-tier supplier,’ *Journal of Operations Management* 41 (2016) 42-60, p. 44. This is confirmed in European Commission, ‘Study on Due Diligence Requirements Through the Supply Chain. Final Report,’ 2020, [op.europa.eu/en/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75e-d71a1](https://op.europa.eu/en/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75e-d71a1), p. 181.

30 See, e.g., B.L. MacCarthy et al., ‘Mapping the supply chain: Why, what and how?,’ *International Journal of Production Economics* 250 (2022) 108688, p. 2, 16; and M.S. Mubarik, N. Naghavi, M. Mubarik et al., ‘Resilience and cleaner production in industry 4.0: Role of supply chain mapping and visibility,’ *Journal of Cleaner Production* 292 (2021) 126058, p. 2, 8.

31 M. Wilhelm et al., ‘Implementing sustainability in multi-tier supply chains: Strategies and contingencies in managing sub-suppliers,’ *Int. J. Production Economics* 182 (2016) 196–212, 197. See also United Nations Global Compact, *A Guide to Traceability. A Practical Approach to Advance Sustainability in Global Supply Chains* (2014, [unglobalcompact.org/library/791](https://unglobalcompact.org/library/791)).

32 Villena 2018, 66.

33 With regard to the power and dependency dynamics of suppliers and customers, see M. Tachizawa, E. and Yew Wong, C. (2014), ‘Towards a theory of multi-tier sustainable supply chains: a systematic literature review,’ *Supply Chain Management*, 19(5/6), pp. 643-663.

34 Zie Cafaggi 2016, p. 242.

35 V.H. Villena & D.A. Gioia, ‘A More Sustainable Supply Chain’, *Harvard Business Review*, March-April 2020, p. 88.

supply chains.<sup>36</sup> However, it does not explain how the Directive will meet these challenges other than claiming that a harmonized, horizontal instrument will offer legal certainty to businesses.<sup>37</sup>

This gap, therefore, calls for a closer examination of the requirements of the reality of trading signs for the effectiveness of a contractual control of chain participant behavior. Codes of conduct, action plans, and commercial contracts, including chain clauses, are only part of a broader pallet of legal relationships and forms of cooperation. Anyone who observes the current use of corporate social responsibility clauses (“CSR clauses”), which we will do next, will quickly conclude that it is also necessary to use other instruments to promote the sustainability of supply chains.<sup>38</sup>

## 4. Purchase and sales terms and conditions in practice

### 4.1. Introduction

Under Article 12 of the proposed Directive, the Commission has to issue Guidelines to increase the effectiveness of contractual clauses. In this section, we will make some suggestions for those Guidelines, taking into account (i) the requirements for contractual assurances that we derive from the proposed Directive, in particular Articles 7 and 8 thereof, (ii) examples of contractual clauses currently used by various multinational companies and (iii) reports that have appeared in recent years on the problems that will have to be overcome in the practice of supply chains for such sustainability clauses to be effective. These studies offer key insights that are becoming available only recently. Traditionally, sustainable supply management studies have focused on the relationship between the buying company and its direct, tier-1 suppliers. Only recently have scholars started taking a multi-tier approach to study the challenges and possibilities of supply chain management that extends to lower-tier suppliers as well.<sup>39</sup>

We looked at the purchase and sales terms of twelve multinational companies published on the companies’ websites. The proposed Directive targets neither a particular type of contract nor a specific sector. It focuses on the company’s specific role in the supply chain. Therefore, we looked at both purchase and sales terms, which do not necessarily involve purchasing or selling movable goods. They may also include services. In all these situations, companies can influence sustainability to be practiced in the supply chain.

According to their websites, eleven out of twelve companies have a code of conduct drawn up with corporate social responsibility in mind.<sup>40</sup> They have a supplier’s code of conduct. We zoom in on the contracts because these lay down the mutual obligations of the company and its business partners. However, we will refer to the supplier’s code of conduct if it contains text that indicates an enforceable obligation of the supplier.

We recognize that the companies involved do not always stick to the terms as published on their websites and that they may customize their agreements. Therefore, our inventory does not purport to assess the terms and conditions used. Instead, our survey merely examines whether they already cover the issues raised by the Directive and whether the Commission can draw inspiration from them, given the task assigned to it by Article 12.

<sup>36</sup> Explanation to the Proposal, p. 2.

<sup>37</sup> Explanation to the Proposal, p. 2-3, 16.

<sup>38</sup> This is also the tenor of the deliberations on directive proposals in the Dutch Parliament; TK 2021–2022, 22 112, nr. 3429 (Report of a written consultation), p. 8, 17. See also the werkgroep Beoordeling Nieuwe Commissie voorstellen (BNC), EK 2021–2022, 22 112, IS (Letter from the minister van buitenlandse zaken), p. 6-7.

<sup>39</sup> See, e.g. M.M.C. Fritz, ‘A supply chain view of sustainability management,’ *Cleaner Production Letters* 3 (2022) 100023, p. 1; Villena 2018, 65.

<sup>40</sup> ASML refers to the Code of Conduct of the Responsible Business Alliance.

## 4.2. The extent of sustainability obligations

As summarized in paragraph 2, the proposal directive implicitly defines various requirements for commercial contracts. The first two are of a general nature:

- The contract must provide provisions on the sustainability of the production process in the supply chain.
- The contract provides for specific consideration of the potential negative consequences and the realized negative consequences of the agreement to be concluded.

The first requirement merely puts the sustainability of the supply chain on the agenda; the second follows from the distinction of Articles 7 and 8.

All of the purchase terms and conditions we examined give some attention to the requirements for supply chain sustainability. The companies refer to their own codes of conduct and ask their suppliers to subscribe to and comply with them. They also simply state that the code of conduct is part of the contract, like the Volkswagen Group does in the VW AG/Procurement Division General Terms and Conditions for Purchasing:

‘3.3 Unless otherwise agreed, the most current versions valid at the time of contract conclusion, including the Specifications for Production Equipment, as well as the contractual terms for customs and foreign trade law the Volkswagen Group requirements regarding sustainability in relationships with business partners (Code of Conduct for Business Partners) shall be made elements of the contract.’

In their purchase terms, none of the companies make a distinction between the potential negative consequences and the realized negative consequences of the agreement to be concluded, which the proposed Directive calls for in Articles 7 and 8.

Research shows that the codes of conduct to which contractual commitments refer must be sufficiently concrete. Clauses usually cover the environment, human rights, working conditions, corruption, and health and safety. In three-quarters of cases they provide for general principles rather than concrete objectives.<sup>41</sup> Moreover, these principles are neither discussed specifically during negotiations nor focused on the specific relationship, suppliers, or business sector.<sup>42</sup> Thus, it is not inconceivable that the CSR clauses are not sufficiently noticed and therefore, not applied as a guide for the supplier’s business decisions.<sup>43</sup>

There is a big difference between purchase and sales terms and conditions regarding the attention given to contractual sustainability obligations. None of the terms of sale refers to the company’s own code of conduct, let alone to the expectations that could be derived from it.<sup>44</sup> At most, it is specified in general terms that the products or services provided will not be used in a way that damages the company’s good name. On the contrary, companies stipulate that the terms of sale take precedence over deviating purchase conditions of the other party. If such a clause is effective, it will never contribute to a more sustainable supply chain. After all, the supply chain does not necessarily end with the agreement between the company as a buyer and its counterparty as a supplier. Yet, it should be obvious that companies, if one accepts their responsibility in the supply chain for countering the negative impact of activities, make commitments similar to the terms of sale that they impose on their suppliers.

41 EcoVadis & Affectio Mutandi, ‘Sustainability Clauses in Commercial Contracts: The Key to Corporate Responsibility. 2018 Study of CSR Contractual Practices Among Buyers and Suppliers’, 2018, p. 23., p. 14, 19, 50, <https://resources.ecovadis.com/whitepapers/sustainability-clauses-commercial-contracts-key-corporate-responsibility>.

42 S. Barrad et al., ‘The Application of System Dynamics for a Sustainable Procurement Operation,’ in H. Quadrat-Ullah (ed.), *Innovative Solutions for Sustainable Supply Chains*. Springer International Publishing (2018), p. 186; EcoVadis & Affectio Mutandi 2018, p. 35, 37-40.

43 Zie EcoVadis & Affectio Mutandi 2018, p. 38.

44 We were not able to check the general conditions of sale of VW.

We, therefore, recommend that the Commission's Guidelines include guidance on both purchasing and selling terms explicitly. Furthermore, it should stress that contract terms on sustainability should preferably be as specific as possible, distinguishing between the potential and known adverse effects of the contract being negotiated.

### **4.3. Influence on admission and expulsion of chain participants**

The Proposal Directive does not impose requirements on the choice of business partners. In practice, however, the extent to which the company can prevent or mitigate the negative impact of its business activities will depend to a large extent on whom it partners.

First, in terms of its direct business relationship - the so-called tier-1 suppliers - the company's "choice of partner" is crucial for achieving sustainability that extends to the underlying chain participants. After all, if the tier-1 supplier's commitment to a sustainable supply chain is reliable, it reduces the likelihood that subsequent chain participants are not.<sup>45</sup>

It is also vital for the company to be able to influence who is allowed into the chain, that is, who the business partners of its directly established business associates are - and perhaps the underlying business associates. So here we are talking about making the supply chain more sustainable by influencing the entry and exit of the chain.<sup>46</sup> To this end, the company must obtain information from its direct business partner about the suppliers of their suppliers. Furthermore, the access criteria shouldn't merely focus on considerations of cost, quality, or delivery - which is still too often the case in practice; they should also include sustainability obligations.<sup>47</sup>

Several of the codes of conduct we examined express the expectation that suppliers undersign the code explicitly. Apparently, sustainability requirements are not merely meant to be a matter of general terms and conditions. Yet, the terms and codes do not make clear whether, in addition to the signature, information is actively acquired about the supplier's business partners. An exception is the Responsible Sourcing Policy of Unilever, distinguishing between suppliers that comply with the minimum standards of its policy and further suppliers with good and best practices. To reach the level of good practices, the supplier's business partners are explicitly examined from the sustainability perspective.<sup>48</sup>

Accordingly, we recommend that the Commission's future Guidelines address the selection of contract partners.

### **4.4. The content and scope of commitments to sustainability**

The core of the proposed Directive, as shown in paragraph 2, lies in the sustainability commitments to be stipulated. We were able to derive the following requirements:

- The contract contains obligations to comply with the company's code of conduct and action plan,
- The contract pays attention to the supply chain; compliance with the code of conduct and action plan must be passed on to other links in the supply chain.

As mentioned earlier, all purchase terms and conditions we examined contain a commitment to comply with the company's code of conduct. A few ask verbatim for a guarantee or "warranty" rather than any commitment or "assurance" as required by the Proposal Directive.<sup>49</sup>

<sup>45</sup> EcoVadis & Affectio Mutandi 2018, p. 23.

<sup>46</sup> Cafaggi 2016, p. 233.

<sup>47</sup> Veronica H. Villena, 'The Missing Link? The Strategic Role of Procurement in Building Sustainable Supply Networks,' *Production and Operations Management Society* 28(5), May 2019, pp. 1149–1172, p. 1151, 1166; Forrester, 'Seize The CSR Opportunity. The State Of Corporate CSR And How To Propel It Forward', 2021, p. 16, 17, <https://info.ivalua.com/forrester-corporate-social-responsibility>.

<sup>48</sup> Parts 1.8 and 1.9 of Chapter II. (Continuous improvement, benchmarks) van de Responsible Sourcing Policy.

<sup>49</sup> Art. 15(1)(d) Royal FrieslandCampina; art. 15 Heineken.

Most of the purchase terms and conditions do not reflect the use of action plans as envisaged by the proposed Directive with an eye on the cases where the potential negative impacts necessitate such a plan. They should be adjusted accordingly. An exception can be found in the general purchase conditions of goods and/or services of the French company Alstom. Clearly induced by the French Duty of Care Law (2017-399) article 25.1.2.2 demands:

‘upon Purchaser’s request, the Supplier shall provide the Purchaser with an assessment delivered by a qualified body reasonably acceptable to the Purchaser, evaluating Supplier’s Corporate Social Responsibility risks. The Supplier undertakes to implement the necessary preventive corrective and remedial actions and warrants to maintain in place, throughout the term of the Contract and/or the Order(s), risk assessment and prevention improvement plans aiming at preventing serious violations with respect to human rights and fundamental freedoms, health and safety of persons and the protection of the environment.’

Most purchase terms and conditions pay little attention to the supply chain, while compliance with the code of conduct and action plan should be passed on to other business partners in the supply chain.

KPN’s do, in a straightforward way, albeit limited to the first tier:

‘Article 5 Corporate Social Responsibility

The supplier will comply with the latest version of KPN’s Supplier Code of Conduct (<https://www.kpn.com/general/all-conditions.htm>) and ensure that its personnel, subsidiaries, and subcontractors comply with all applicable legislation.’<sup>50</sup>

In its purchase terms and conditions, Unilever generally limits the obligation to the group of companies to which the supplier belongs:

‘6.1. Supplier acknowledges that it has read the Unilever Responsible Sourcing Policy (the ‘RSP’) ... Supplier agrees a) that all entities of the Supplier group will comply with the Mandatory Requirements set out in the RSP (the ‘Mandatory Requirements’).’

Concerning the presence of “conflict minerals,” the obligation extends to the supply chain:

‘6.4 ... Supplier must perform appropriate due diligence on its supply chain in order to identify the actual presence and origin of conflict minerals in any product no later than thirty (30) days following each calendar year’.

The various Supplier Codes of Conduct offer more information. For example, the Randstad Global Supplier Code has a firm and generally worded provision:

‘The conditions of the Code are also applicable to the supplier’s own supply base (sub-suppliers and subcontractors), and the supplier is accountable for ensuring that compliance is assured across all aspects of supply. Randstad reserves the right to amend the Code’.

Alstom explicitly requires its Suppliers and Contractors:

‘to represent and warrant to cascade the principles contained in this Charter for Ethics and Sustainable Development to their own suppliers and contractors and to implement a similar continuous improvement and compliance approach.’<sup>51</sup>

<sup>50</sup> Also the *Gedragcode voor Zakenpartners of AkzoNobel* limits the obligation to subcontractors.

<sup>51</sup> Ethics and Sustainable Development Charter for Alstom’s suppliers and contractors.



Unilever refers to the supplier's codes; they must be consistent with its own Responsible Sourcing Policy:

'The supplier has in place a code of conduct or responsible sourcing policy for its direct suppliers, which is consistent with the requirements of this Responsible Sourcing Policy. In addition, there is a process to communicate the requirements of the supplier's code or policy to all of its direct suppliers and to monitor compliance by these direct suppliers'.

DSM and Heineken are somewhat modest by expressing the expectation that their code will be observed further down the supply chain. Shell chooses an indirect formulation; its Supplier Principles state that Shell will develop and strengthen relationship ties with suppliers who commit to the Principles, taking them into account in their own business decisions and in the relationship with their suppliers.

General research on the practice of supply chains lowers the expectations of the effect of clauses that intend to govern the supply chain. While such contractual instruments are ideally suited to implement the code of conduct beyond the direct business relationship, i.e., the tier-1 suppliers, compliance with chain clauses beyond the first link is often disappointing.<sup>52</sup> For example, a recent study conducted by EcoVadis and Affectio Mutandi shows that less than half of the CSR clauses used by the companies they studied contained a chain clause beyond the first tier.<sup>53</sup> The likelihood of success of chain commitments might be higher if the company actively engages the direct business relationship to play a more active role, including making the necessary investments to bolster the tier-1 suppliers' unique role as midway facilitators between the company and the lower-tiers supply chain.<sup>54</sup> Furthermore, through investing resources in developing human resource training, the company can play a key role in raising awareness and promoting sustainable conduct in its supply chain.<sup>55</sup> Offering suppliers training increases the likelihood that the latter will also help underlying chain participants implement sustainability commitments<sup>56</sup> and further the exchange of best practices.<sup>57</sup> This approach could be linked to the surveillance mechanism in place, about which Section 4.6 elaborates.

Research also shows that attention must be paid to the compatibility between the sustainability requirements and requirements for the products and services to be provided. For example, it is challenging to ensure working conditions concerning the maximum number of working hours per week if the company sets unrealistic delivery deadlines simultaneously.<sup>58</sup> Suppliers appear to consider such sustainability requirements reasonable, but the cost aspect clearly needs attention.<sup>59</sup>

Therefore, we recommend that the Commission's Guidelines address the issue of the content, scope, and embedding of mandatory contractual commitments.

52 V.H. Villena & D.A. Gioia, 'On the riskiness of lower-tier suppliers: Managing sustainability in supply networks,' *Journal of Operations Management* 64 (2018) 65–87, p. 81. See, also, European Commission, 'Study on due diligence requirements through the supply chain. Final Report', 2020, <https://op.europa.eu/en/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75ed71a1/language-en>, p. 16.

53 EcoVadis & Affectio Mutandi 2018, p. 22.

54 Wilhelm et al. 2016, p. 55, who dub the tier-1 supplier's position the 'double-agency' rol.

55 T. Borges Teixeira et al., 'Sustainability in the Supply Chain: Analyzing the Role of the Focal Company and Training in the Implementation of SDGs,' *Sustainability* 2022, 14, 12882, p. 12.

56 Villena & Gioia 2018, p. 83.

57 Villena & Gioia 2018, p. 77, 78.

58 Villena & Gioia 2020, p. 88.

59 EcoVadis & Affectio Mutandi 2018, p. 31.

#### 4.5. Deployment of the termination power

The proposed Directive requires commercial contracts to include a termination option if sustainability efforts come to nothing, albeit termination is regarded as an *ultimum remedium* (see paragraph 2). We derive the following requirements from this:

- The contract provides for termination of the contractual legal relationship if there is a potentially severe adverse effect from a sustainability perspective.
- The contract views termination of the contractual relationship as a last resort.

In the purchase terms and conditions that we examined, termination of the contractual relationship due to potentially severe adverse effects is not elaborated upon extensively.<sup>60</sup> There is little attention altogether to the consequences of non-performance of the commitment. Finally, it does not follow from any set of purchase terms and conditions that termination of the legal relationship is seen as a last resort.

The DSM terms and conditions are an exception:

##### '17. Termination and suspension

17.1 Customer is entitled to suspend the performance of its obligations in whole or in part or terminate the Agreement with immediate effect, without prejudice to its right to claim damages and without any compensation to or indemnification of Supplier...

(ii) in case of noncompliance with clause 4, including but not limited to, the DSM Supplier Code of Conduct.'

According to art. 27.2 of the Ericsson Purchasing Conditions, Ericsson may terminate the Agreement immediately if the supplier has breached the Ericsson Code of Conduct for Business Partners. If Ericsson:

'reasonably and in good faith believe that there may have been a breach of (...) the Ericsson Code of Conduct for Business Partners (...), or such breach is likely to occur, by Supplier (...), Supplier must at its own cost cooperate fully with Ericsson to determine whether such a breach has occurred, or, if it is likely to occur, take action to prevent the occurrence of such breach. Ericsson may, upon written notice, withhold further payments to Supplier under the Agreement until such time as it has been determined to Ericsson's satisfaction that no such breach has occurred or is likely to occur'.

Implicitly, the issue comes up in the Randstad terms and conditions, wherein noncompliance with the code is considered a default. That qualification opens the way to termination if the shortcoming would justify it (Section 6:265(1) BW):

##### '18. Randstad Group supplier code

18.1. The supplier shall comply with the 'Randstad Group supplier code' attached to these General Terms and Conditions and any amendments thereto insofar as it has been made known to the supplier. Noncompliance with the Randstad Group supplier code shall be considered a material breach of this agreement by the supplier.

AkzoNobel states in the first paragraph of its Business Partner Code of Conduct that failure to comply with the Code may result in action, including termination of the business relationship. KPN, in its Supplier Code of Conduct, stops short of reconsidering the legal relationship: 'KPN may reconsider its relationship with a supplier that does not comply with this code.'

<sup>60</sup> Compare EcoVadis & Affectio Mutandi 2018, p. 48.

In none of the terms examined do we come across a power that allows the company to prohibit its business partners from dealing with the same supplier in the future, thus rejoining the chain.<sup>61</sup> However, such an interpretation of a termination clause may offer the company greater leverage in the admission and expulsion of chain participants that we discussed above (Section 4.3).

Including the power to terminate a contract, as these examples do, could serve several goals. First, such a clause enables the company to remove business partners from the supply chain if they do not take sustainability seriously. However, that power should serve primarily not as a contractual sanction but as a means of promoting behavior change. In addition, linking sanctions to the CSR obligation can also increase the supplier's awareness that the CSR clause is legally binding and enforceable, not mere window-dressing, thus leading to a higher level of compliance.<sup>62</sup> Without such a link, suppliers may consider the focus on sustainability merely a communication tool.<sup>63</sup>

Furthermore, contractual remedies should not merely address individual instances of noncompliance but focus on structural failures.<sup>64</sup> Studies show that although CSR clauses often mention termination as the consequence of noncompliance, only a small proportion of companies actually do terminate the contract in case of noncompliance with CSR clauses.<sup>65</sup> In this regard, the power of rescission appears to be more effective in making the supply chain more sustainable if CSR clauses include a gradual penalty system that indicates the escalating consequences of noncompliance, ranging from an obligation to set up an action plan to correct the wrongs, to suspension of the contract, forfeiture of contractual penalties (which can also be calculated incrementally), and finally, dissolution.<sup>66</sup> Thus, sustainability appears to be a matter of both the purchaser and the supplier instead of a risk for the supplier solely.<sup>67</sup>

Finally, it is essential not to focus purely on penalties for violation of CSR clauses. Suppliers that perform well should be rewarded. In other words, in addition to contractual "sticks," contractual "carrots" can also be effective. For example, CSR clauses can include commercial incentives such as conditional price increases, increases in volumes to be purchased or frequency of purchase, contract extensions, and the granting of preferential positions.<sup>68</sup> A company may also offer suppliers positive incentives through scorecards and preferred-supplier or sustainability award programs.<sup>69</sup> These initiatives may also induce a level of competition among suppliers in terms of improving the sustainability of their operations.<sup>70</sup> Moreover, as the effects of a company's coercive market power diminish further down its supply chain, employing its capacity to issue rewards becomes an increasingly effective alternative.<sup>71</sup>

The preceding analysis termination of the contractual relationship related to sustainability commitments deserves further elaboration in the Guidelines. In addition, embedding the termination option in a broader context of remediation could be linked to a monitoring mechanism. On the latter, see the next section.

61 Cafaggi 2016, p. 234.

62 EcoVadis & Affectio Mutandi 2018, p. 15, 48-49.

63 EcoVadis & Affectio Mutandi 2018, p. 49.

64 Cafaggi 2016, p. 228.

65 EcoVadis & Affectio Mutandi 2018, p. 48.

66 Cafaggi 2016, p. 224, 246-7. EcoVadis & Affectio Mutandi 2018, p. 15, 52-4.

67 EcoVadis & Affectio Mutandi 2018, p. 25.

68 John G. Ruggie, 'From Audit to Innovation. Keynote Address at the Annual Conference of the Business Social Compliance Initiative Former UN Special Representative for Business & Human Rights Brussels', 2014, p. 4, <https://www.hks.harvard.edu/sites/default/files/centers/mrcbg/programs/crj/files/BSC1%2BKeynote.pdf>. See also EcoVadis & Affectio Mutandi 2018, p. 52.

69 Villena 2019, p. 1159.

70 Villena & Gioia 2018, p. 75.

71 See O.A. Meqdadi et al., 'Power and Diffusion of Sustainability in Supply Networks: Findings from Four In-Depth Case Studies,' *J Bus Ethics* 159, 1089–1110 (2019), p. 1105.

#### **4.6. A balanced monitor mechanism**

Under the terms of the proposed Directive, companies must not only be mindful of the commitments they are required to stipulate but must also monitor compliance with those commitments. From this, we derive the final requirements that contracts must meet:

- The contract provides for a fair, reasonable, and non-discriminatory monitoring mechanism.
- The contract considers the particular position of SME partners.
- The contract provides that the costs of the monitoring mechanism will be borne by the company and not by small and medium-sized enterprise partners.
- The contract provides for flanking policies to support SME partners.

Most purchase terms and conditions we reviewed have a general inspection option. However, none of the purchase terms and conditions or Supplier Codes of Conduct show any consideration for business partners from small and medium-sized enterprises, let alone the provision of a lenient oversight mechanism and flanking policies for these business partners. Thus, the payoff is paltry.

KPN and Randstad address the issue in their Supplier Code of Conduct, which shows that suppliers are given time to make improvements. In addition, in the Heineken Supplier Code, Heineken offers “tips” for compliance:

‘We recognize that we have a duty to support our Suppliers to help improve standards and capabilities. The introduction of the tips for continuous improvement sections act as a reference and offers support on how to further improve on the respective fields of responsible business conduct in this Supplier Code.’

In its Code of Conduct for Business Partners, Ericsson offers online training courses:

‘We understand the complexity in the supply chain and are committed to engaging with our Business Partners to ensure continuous and measurable improvements over time. As a part of this commitment, we offer training and support for our Business Partners on the content and the obligations defined within the Code’.

DSM hints in its Supplier Code of Conduct at support for supplier compliance:

‘Through dialogue with our suppliers, and training if required, we aspire to achieve an adequate implementation of the Supplier Code of Conduct, to continuously improve business conduct and to discover our suppliers’ unique competences that contribute to People, Planet and Profit.’

Unilever, contrary to what the Directive will require, charges the cost of monitoring to the other party:

‘6.1. ... Supplier agrees: ... b) to take at its own cost any action reasonably required by Unilever to: (i) verify compliance by all entities of the Supplier group with the Mandatory Requirements; and (ii) rectify any noncompliance by an entity of the Supplier group within the timeframe stipulated by Unilever.’

According to the Volkswagen Code of Conducts for Business partners the supplier is responsible for remedying such non-compliance at no additional cost to the Volkswagen Group. Yet, Volkswagen has a protected whistleblower system in place, which may be used by suppliers, including an internet-based communication platform, confidential and protected, for contacting lawyers working in the Investigation Office, exchanging documents and staying in touch via a separate mailbox. This platform is confidential and protected. Furthermore external ombudspersons are available as a point of contact. These are lawyers who are bound by the oath of professional secrecy, including towards Volkswagen Group.

It makes sense for the guidelines to address the monitoring mechanism explicitly. A contractual balance on this point benefits the sustainability of the supply chain in at least three respects.

First, the proposed Directive did well to require the company to bear at least part of the cost of suppliers' compliance with CSR clauses or provide assistance, including the cost of conducting CSR compliance monitoring. Indeed, in reality, complying with CSR clauses regularly poses operational problems for suppliers. Research shows that they often lack the necessary resources and expertise, and compliance with CSR clauses is impossible without compromising production levels' maintenance.<sup>72</sup> In particular, suppliers lower down the supply chain seem to be operationally less able to comply with CSR obligations set at the top of the chain. They tend to be well-informed about such obligations, and lack the necessary expertise and sufficient resources.<sup>73</sup> However, most companies have suppliers bear the total cost of audits. A smaller proportion of companies share the costs, but few pay the costs entirely themselves.<sup>74</sup> Beyond adopting a cost-sharing approach, the company may also lessen the financial burden on suppliers by lowering the overall monitoring cost. They can, for example, develop a selective monitoring approach based on a risk analysis that identifies suppliers that hold an influential position in the supply chain or are most likely to commit a wrongdoing.<sup>75</sup>

Second, CSR clauses prove to be more effective if they include a concrete obligation for suppliers to tolerate or conduct audits or assessments.<sup>76</sup> Research shows that companies have great difficulty in monitoring compliance with CSR clauses.<sup>77</sup> On this point, too, the proposed Directive does well to seek a balanced monitoring mechanism. Inadequate monitoring by the entrepreneur in the chain is critical in effectuating CSR commitments throughout the supply chain.<sup>78</sup> Therefore, CSR clauses better include a concrete obligation for suppliers to allow audits or assessments by audit companies or, albeit a less reliable alternative, perform self-assessments themselves.<sup>79</sup> However, studies indicate that monitoring is more effective when they are not so much part of a compliance-based approach but rather a cooperation-based strategy that focuses on the parties' interdependence and, thus their long-term, trust-based relationship.<sup>80</sup>

---

72 EcoVadis & Affectio Mutandi 2018, 35, 51.

73 Villena & Gioia 2018, p. 66.

74 EcoVadis & Affectio Mutandi 2018, 15, 44.

75 EcoVadis & Affectio Mutandi 2018, 43, 45

76 EcoVadis & Affectio Mutandi 2018, 44.

77 EcoVadis & Affectio Mutandi 2018, 43

78 K. Govindan et al., 'Social sustainability tensions in multi-tier supply chain: A systematic literature review towards conceptual framework development,' *Journal of Cleaner Production* 279 (2021) 123075, p. 7, 19.

79 EcoVadis & Affectio Mutandi 2018, 43, 44.

80 P. Lund-Thomsen & A. Lindgreen, 'Corporate Social Responsibility in Global Value Chains: Where Are We Now and Where Are We Going?', *J Bus Ethics* (2014) 123:11–22, p. 12-6.

Third, CSR clauses should avoid placing all risks of reputational damage or third-party compensation claims on the supplier.<sup>81</sup> If it were factually and legally tenable to shift responsibility from company to supplier, it would be because of the adverse effects on the willingness of suppliers and other business partners to contribute to increasing sustainability in the supply chain. Indeed, this imbalance would cause suppliers to refrain from further cooperation with the company.<sup>82</sup>

How supervision should be framed through commitments, especially considering the distribution of the costs involved and the risks in case of noncompliance with the codes of conduct, therefore, deserves elaboration in the Guidelines in relation to the substantive commitments discussed in section 4.4 and with the sanctions in section 4.5.

#### **4.7. The importance of cooperation**

The proposed Directive, both in Articles 7 and 8 and in the preamble and explanatory memorandum to the Directive, demonstrates an awareness of the importance of a collaborative effort of companies, their suppliers, and other entities in making supply chains sustainable. However, what this cooperation should entail in practice and how it can be achieved is not explained by the Directive. Some Codes of Conduct offer a starting point, as evidenced by the examples of DSM and Heineken from the previous section. Research conducted in recent years by social science scholars and interest groups offers some perspective.

First, cooperation between companies and their tier-1 suppliers appears effective. Such collaboration requires, for example, a fair allocation of responsibilities.<sup>83</sup> For example, there are examples of consumer goods manufacturers helping their supplier design and implement sustainability programs.<sup>84</sup> Such a collaborative attitude fits well with the value of fostering long-term business relationships with their suppliers.<sup>85</sup> When companies invest in long-term contractual relationships with their suppliers, developing the required sustainable procedures and practices will be worth the suppliers' investment.<sup>86</sup>

Second, a form of collaboration that promotes sustainability in the supply chain is admitting suppliers as members of the trade association of which the company is a member. This way, through their membership, these suppliers are directly obligated to meet their customer's exact sustainability requirements.<sup>87</sup> Moreover, cooperation among companies competing within the same market works to save costs for themselves and their suppliers. For example, where supply chains overlap, companies can collaborate in the form of global industry associations.<sup>88</sup> In this way, sustainability requirements can be standardized within particular economic sectors.<sup>89</sup> In this way, sector-wide uniform standards prevent suppliers from simultaneously complying with different or sometimes conflicting CSR clauses.<sup>90</sup> Additionally, through these associations, companies can jointly organize and share the costs of monitoring compliance with CSR clauses by suppliers they have in common.<sup>91</sup> Moreover, the supplier's interest in complying with the codes of conduct will be vital if noncompliance with one buyer's code of conduct also means noncompliance with that of other buyers.<sup>92</sup> Chain participants might also be more likely to act when called upon by multiple customers.<sup>93</sup>

81 EcoVadis & Affectio Mutandi 2018, p. 52. Compare TK 2021–2022, 22 112, nr. 3429 (Report of a written consultation), p. 6, 7, 16-7, 32-3. Letter dated June 24, 2022 from De vaste commissie voor Buitenlandse Zaken, Defensie en Ontwikkelingssamenwerking, 'Vragen inzake het BNC-fiche over het voorstel voor een Richtlijn inzake passende zorgvuldigheid in het bedrijfsleven op het gebied van duurzaamheid', p. 2. See also the werkgroep Beoordeling Nieuwe Commissie voorstellen (BNC), EK 2021–2022, 22 112, IS (Brief van de minister van buitenlandse zaken), p. 6.

82 EcoVadis & Affectio Mutandi 2018, p. 45.

83 EcoVadis & Affectio Mutandi 2018, p. 52.

84 Bové & Swartz 2016, p. 7.

85 EcoVadis & Affectio Mutandi 2018, p. 50.

86 Planbeck 2012, p. S66-S67.

87 Villena 2019, p. 1166.

88 Bové & Swartz 2016, p. 7; Villena & Gioia 2020, p. 91-2.

89 Villena 2019, p. 1166.

90 EcoVadis & Affectio Mutandi 2018, p. 45.

91 See Cafaggi 2016, p. 242.

92 See, indirectly, Cafaggi 2016, p. 241.

93 CDP 2021, p. 26

Third, entrepreneurs should be induced to work with governments, NGOs, and other civil society partners at the global level. This strategy is particularly important for overcoming the biggest obstacle in companies' control of their supply chains: traceability or visibility of participants' activities lower down the chain, at least further away from the customer.<sup>94</sup> Entrepreneurs can gather information about underlying chain participants through their tier-1 suppliers.<sup>95</sup> At this moment, however, this does not seem to happen often enough. Cooperation with private, public, and social partners to gather information can thus address the problem of traceability.

As far as we are concerned, it would be helpful if the guidelines to be drawn up by the Commission included guidelines for developing cooperation within sectors, within and between supply chains, and with different stakeholders to exchange information and promote monitoring.

## **5. Conclusion**

We are less than confident about the expected contributions the proposed Directive will offer to prevent, reduce, and eliminate environmental damage and human rights violations caused by the activities of global business. The Directive's assured use of contractual assurances and monitoring activities in the supply chain might not be warranted. While it is conceivable that the penalty and civil liability provisions may incentive companies to follow the Directive's contractual requirements, that effect will not necessarily make the use of contracts successful in reducing the adverse effects of global supply chains. Still, insights from current contracting practices hopefully offer a first step toward making the supply chains of companies in the European Union more sustainable in reality.

We, therefore, recommend that the guidelines to be developed by the Commission under Article 12 of the proposed Directive will include guidance on the level of detail of assurances in terms and conditions of purchase and sale and codes of conduct, the influence of companies on the entry and exit of suppliers in the supply chain, the connecting of monitoring mechanism with the consequences of noncompliance, the balance of the allocation of costs of monitoring and the risks of noncompliance with attention to the position of SME business partners, and the horizontal and vertical cooperation in the web of buyers and suppliers can be most effectively designed.

---

<sup>94</sup> Cafaggi 2016, p. 228-229, 238. European Commission 2020, p. 70 e.v.

<sup>95</sup> Cafaggi 2016, p. 229, 238.

## List of procurement terms and conditions and Supplier Codes of Conduct consulted

AkzoNobel, Algemene Inkoopvoorwaarden

[www.akzonobel.com/content/dam/akzonobel-corporate/global/en/about-us/for-suppliers/terms-and-condition-global-terms-and-condition-of-purchase-akzonobel.pdf](http://www.akzonobel.com/content/dam/akzonobel-corporate/global/en/about-us/for-suppliers/terms-and-condition-global-terms-and-condition-of-purchase-akzonobel.pdf)

[www.akzonobel.com/en/about-us/governance-/policies---procedures/business-partner-code-of-conduct0](http://www.akzonobel.com/en/about-us/governance-/policies---procedures/business-partner-code-of-conduct0)

Alstom general purchase conditions of goods and/or services (Standard Version Direct Domains)

[www.alstom.com/suppliers/general-purchase-conditions?page=3](http://www.alstom.com/suppliers/general-purchase-conditions?page=3)

[www.alstom.com/sites/alstom.com/files/2018/07/16/ethics\\_and\\_sustainable\\_development\\_charter\\_for\\_alstoms\\_suppliers\\_and\\_contractors\\_.pdf](http://www.alstom.com/sites/alstom.com/files/2018/07/16/ethics_and_sustainable_development_charter_for_alstoms_suppliers_and_contractors_.pdf)

ASML, Algemene Inkoopvoorwaarden voor goederen en diensten

[www.asml.com/en/general-terms-and-conditions](http://www.asml.com/en/general-terms-and-conditions)

DSM, Algemene inkoopvoorwaarden voor goederen en diensten 2020

[www.dsm.com/content/dam/dsm/suppliers/en/documents/dsm-gpc-2020-nl.pdf](http://www.dsm.com/content/dam/dsm/suppliers/en/documents/dsm-gpc-2020-nl.pdf)

[www.dsm.com/content/dam/dsm/suppliers/en/documents/supplier-code-of-conduct-en.pdf](http://www.dsm.com/content/dam/dsm/suppliers/en/documents/supplier-code-of-conduct-en.pdf)

Ericsson Purchasing Conditions

[www.ericsson.com/491f88/assets/local/about-ericsson/sourcing/documents/conditions-and-guidelines/epc-rev-a-feb-9-2021.pdf](http://www.ericsson.com/491f88/assets/local/about-ericsson/sourcing/documents/conditions-and-guidelines/epc-rev-a-feb-9-2021.pdf)

[www.ericsson.com/4982d3/assets/local/about-ericsson/sustainability-and-corporate-responsibility/documents/supplier-code-of-conduct/ericsson-code-of-conduct-for-business-partners\\_english.pdf](http://www.ericsson.com/4982d3/assets/local/about-ericsson/sustainability-and-corporate-responsibility/documents/supplier-code-of-conduct/ericsson-code-of-conduct-for-business-partners_english.pdf)

Heineken Nederland, Algemene inkoopvoorwaarden

[www.heinekennederland.nl/sites/theheineken-netherlands/files/supplier-portal/inkoopvoorwaarde-n-hnl-2014.pdf](http://www.heinekennederland.nl/sites/theheineken-netherlands/files/supplier-portal/inkoopvoorwaarde-n-hnl-2014.pdf)

[www.theheinekencompany.com/sites/theheinekencompany/files/Suppliers/Heineken-NV-2019-Supplier-Code.pdf](http://www.theheinekencompany.com/sites/theheinekencompany/files/Suppliers/Heineken-NV-2019-Supplier-Code.pdf)

KPN, Algemene inkoopvoorwaarden

[www.overons.kpn/downloads/KPN\\_Algemene\\_Inkoopvoorwaarden\\_General\\_Terms\\_and\\_Conditions\\_of\\_Purchase\\_2022.pdf](http://www.overons.kpn/downloads/KPN_Algemene_Inkoopvoorwaarden_General_Terms_and_Conditions_of_Purchase_2022.pdf)

[www.overons.kpn/downloads/KPN\\_Supplier\\_Code\\_of\\_Conduct\\_2022.pdf](http://www.overons.kpn/downloads/KPN_Supplier_Code_of_Conduct_2022.pdf)

Randstad Groep Nederland, Algemene Inkoopvoorwaarden

<https://www.randstad.nl/binaries/content/assets/randstadnl/over-randstad/2022-01-24-rgn-aiv-met-bijlagen-nl.pdf>

[www.randstad.com/s3fs-media/rscom/public/2021-04/randstad-global-supplier-code-20210412.pdf](http://www.randstad.com/s3fs-media/rscom/public/2021-04/randstad-global-supplier-code-20210412.pdf)



Koninklijke FrieslandCampina, Algemene Inkoopvoorwaarden

[www.frieslandcampina.com/uploads/sites/2/2022/05/Royal-FrieslandCampina-NV-General-Purchase-Conditions-October-2021.pdf](http://www.frieslandcampina.com/uploads/sites/2/2022/05/Royal-FrieslandCampina-NV-General-Purchase-Conditions-October-2021.pdf)

[www.frieslandcampina.com/uploads/2020/04/FrieslandCampina-Compass-Business-practices-for-business-partners.pdf](http://www.frieslandcampina.com/uploads/2020/04/FrieslandCampina-Compass-Business-practices-for-business-partners.pdf)

Shell, Voorwaarden voor de inkoop van goederen en diensten

[www.shell.com/business-customers/shell-for-suppliers/purchase-order-general-t-s-and-c-s/\\_jcr\\_content/par/tabbedcontent/tab\\_597004049/textimage.stream/1632733105302/0bcf0b9a20d01c091d93f01953616034d1888ddc/september-2021-word-editable-version-netherlands.pdf](http://www.shell.com/business-customers/shell-for-suppliers/purchase-order-general-t-s-and-c-s/_jcr_content/par/tabbedcontent/tab_597004049/textimage.stream/1632733105302/0bcf0b9a20d01c091d93f01953616034d1888ddc/september-2021-word-editable-version-netherlands.pdf)

[www.shell.com/business-customers/shell-for-suppliers/supplier-principles.html](http://www.shell.com/business-customers/shell-for-suppliers/supplier-principles.html)

Unilever, Algemene voorwaarden voor de aankoop van producten en diensten

[www.unilever.nl/files/origin/7344b278c56ecf7d82535805618364039f87f494.pdf/2021-03-Global-purchasing-GTCs-English.pdf](http://www.unilever.nl/files/origin/7344b278c56ecf7d82535805618364039f87f494.pdf/2021-03-Global-purchasing-GTCs-English.pdf)

[www.assets.unilever.com/files/92ui5egz/production/9cc1fed0d3248247089934dac59383022833a162.pdf/slp-unilever-responsible-sourcing-policy-2014.pdf](http://www.assets.unilever.com/files/92ui5egz/production/9cc1fed0d3248247089934dac59383022833a162.pdf/slp-unilever-responsible-sourcing-policy-2014.pdf)

VW AG/Procurement Division General Terms and Conditions for Purchasing (current as of 18 February 2021)

[www.vwgroupsupply.com/one-kbp-pub/media/shared\\_media/documents\\_1/einkaufsbedingungen/volkswagen\\_1/einkaufsbedingungen\\_allgemeine\\_beschaffung/allgemeine\\_einkaufsbedingungen\\_vw\\_ag\\_bereich\\_beschaffung\\_allgemein/general\\_terms\\_and\\_conditions\\_of\\_purchase\\_volkswagen\\_ag\\_general\\_purchasing\\_division\\_/2018\\_05\\_01\\_aek\\_eng.pdf](http://www.vwgroupsupply.com/one-kbp-pub/media/shared_media/documents_1/einkaufsbedingungen/volkswagen_1/einkaufsbedingungen_allgemeine_beschaffung/allgemeine_einkaufsbedingungen_vw_ag_bereich_beschaffung_allgemein/general_terms_and_conditions_of_purchase_volkswagen_ag_general_purchasing_division_/2018_05_01_aek_eng.pdf)

[https://www.vwgroupsupply.com/one-kbp-pub/media/shared\\_media/documents\\_1/nachhaltigkeit/brochure\\_volkswagen\\_group\\_requirements\\_regarding\\_sustainability\\_in\\_its\\_relationships\\_with\\_business\\_partners\\_code\\_of\\_conduct\\_fo/Code\\_Of\\_Conduct\\_BP\\_2019.pdf](https://www.vwgroupsupply.com/one-kbp-pub/media/shared_media/documents_1/nachhaltigkeit/brochure_volkswagen_group_requirements_regarding_sustainability_in_its_relationships_with_business_partners_code_of_conduct_fo/Code_Of_Conduct_BP_2019.pdf)

## **Authors**

### **Cornelis J.W. (Jaap) Baaij**

Montaigne Centre for Rule of Law and Administration of Justice;

Molengraaff Institute for Private law, Utrecht University

[c.j.w.baaij@uu.nl](mailto:c.j.w.baaij@uu.nl)

### **Alex Geert Castermans**

Institute of Private law, Leiden University;

Robert Schuman Centre for Advanced Studies, European University Institute

[a.g.castermans@law.leidenuniv.nl](mailto:a.g.castermans@law.leidenuniv.nl) / [ag.castermans@eui.eu](mailto:ag.castermans@eui.eu)