



Sustainability Clauses in Commercial Contracts: The Key to Corporate Responsibility

2018 Study of CSR Contractual Practices Among Buyers and Suppliers

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Executive Summary

New regulations along with consumer and stakeholder pressure regarding sustainability issues have made it crucial for businesses to manage and demonstrate their due diligence on environmental, social and ethical risks in their business relationships, especially in their value chain. As a result, companies, now more than ever, are including Corporate Social Responsibility (CSR)¹ requirements in their contracts, in the form of a so-called sustainability clause or CSR clause.

The need for a CSR clause in commercial contracts has been exacerbated by the 2013 Rana Plaza disaster in Bangladesh, which killed over 1000 sweatshop workers. Many well-known global brands, whose products were found in the wreckage, abruptly discovered that, in the absence of a direct contractual relationship, their “default” due diligence exerted no control over subcontractors. This served as a wakeup call for companies around the world, in all industries.

The international community responded. The guidelines recently published by the OECD covering the garment and footwear sector (2017) and the extractive sector (2016), emphasized the significance of contracts and demonstrated that a CSR clause is the best tool for social and environmental improvement in the supply chain.

Studies on sustainability clauses are scarce, and one of this scale is unprecedented. CSR practices are constantly evolving to respond to changing social and legal pressures. The aim of this study is to give a practical, reality-based overview of current practices. It discusses both, formal considerations, e.g. what should be included in a CSR clause, and operational considerations, e.g. practical consequences of CSR clauses.

The study reflects real-life practice we conducted a survey and analysis of a broad spectrum of both buyers and suppliers to get their insights on the inclusion of CSR into contracts. EcoVadis partnered with Affectio Mutandi to provide expert legal analysis and commentary for the study. We discovered that contracts can significantly contribute to supplier performance improvement and are a powerful tool for CSR and CSR strategy.

¹ The term Corporate Social Responsibility (CSR) is used in this document to refer to the full scope of sustainability topics including environmental, social and ethical practices, as well as monitoring suppliers (sustainable procurement). It is also used interchangeably with the term Environmental, social and corporate governance (ESG).



Key findings include:

- Some 41 percent of suppliers who responded to the survey declared that having CSR requirements in their contracts raised awareness of environmental, social and governance issues;
- Roughly the same proportion believed that it triggered the implementation of concrete actions;
- Of those who did not take any such actions, the majority did not need to do so because they were already following good CSR practices;
- There is a rich variety of different sustainability clauses, with varying levels of effectiveness. Analysis of a wide sample of clauses and of their effects on suppliers, reveals the top four most common weaknesses encountered, and suggested ways to overcome them;
- The study has also led to the design of a diagnostic tool used to measure the effectiveness of a CSR clause. The diagnostic covers four essential elements for a CSR clause, and helps companies to assess and improve their practices and implement consistent contractual diligence mechanisms;
- Also included in the study are a set of Sustainable Contract Principles developed by Affectio Mutandi. The goal of these principles is to guide companies around the world to increase of the use of effective CSR clauses in contracts, which in turn will lead to improved ESG diligence and the positive impacts that it brings.

Edition: June 2018

The quantitative study conducted online among 569 companies from November 16, 2017 to January 12, 2018 was supplemented by in-depth interviews with 20 stakeholders during the same time period.

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Foreword

From Soft Law to Hard Law: A Regulatory Evolution

Soft law offers numerous instruments, which CSR regulations can refer to, from the OECD and ILO guidelines published in the 1970s, to the recent OECD guide for the textile sector, to certificates like Forest Stewardship Council, Max Havelaar, or initiatives such as Roundtable on Sustainable Palm Oil, Responsible Jewelry Council or Together for Sustainability Initiative. Since the 2000s, it has increasingly supported traditional law through judicial and regulatory initiatives introduced in a number of countries.

This “hardening” of norms, initially manifested through increasing transparency demands, which require companies to report on any activities they have undertaken to prevent, mitigate or repair CSR impact in their supply chains. One EU legislation, which is particularly noteworthy, is the 2014 non-financial directive (Directive 2014/95/E). It requires companies with over 500 employees and exceeding a certain turnover level to disclose non-financial information, in addition to financial details, in their reports.

National laws have also adopted transparency obligations regarding the supply chain. They include the California Transparency in Supply Chains Act (2012), The UK Modern Slavery Act (2014), Sapin II (2016), the Child Labor Due Diligence Law in Netherlands (2017), or the Duty of Care Law (Devoir de Vigilance, 2017) in France, which requires large companies to identify and mitigate the risk of corruption, human rights violation, health and safety infringement and environmental damages in their supply chain.

The current legal and regulatory environment, which has evolved over the past 40 years, can be illustrated in the following way:

Voluntary Commitments (Ethics Charters, Codes of Conduct, etc.)

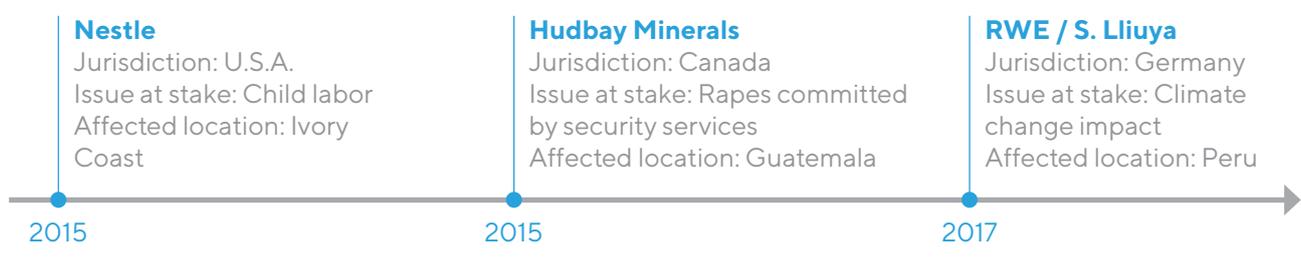




An Increasing Role of OECD National Contact Points



A New Approach: Cross-Border Human Rights Disputes



The Duty of Care Concept Emerges



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On the whole, CSR regulations tend to consider business relationships within the scope of corporate duty of care². The recognition of the corporate duty of care, which requires companies to identify CSR impact of their activities, address it and report on it, places commercial contracts at the core of CSR strategy.



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By organizing business relationships between buyers and suppliers, commercial contracts not only ensure that businesses enter into legally binding agreements, they are also an essential tool to codify the regulatory and societal expectations regarding CSR. Similar to how the *privacy by design* concept developed, which requires personal data to be protected right from the start of any commercial process, the concept of *CSR by design* is emerging. It would require CSR considerations to be included at the outset in commercial contracts.

² The term “duty of care” is used in this document interchangeably with the term ESG/CSR due diligence.

Commercial Contracts as a Key Tool to Enact Duty of Care

“Human rights due diligence should be initiated as early as possible in the development of a new activity or relationship, given that human rights risks can be increased or mitigated already at the stage of structuring contracts or other agreements (...).”

UN Guiding principles on business and human rights, commentary on principle

“(...) Enterprises can also influence suppliers through contractual arrangements such as management contracts, pre-qualification requirements for potential suppliers, voting trusts, and licence or franchise agreements.”

OECD Guidelines for multinational enterprises (2011), comm. 21 on general principles

“Actions enterprises may take to develop policies and management systems are likely to include the following: (...) Incorporate RBC expectations and policies into supplier or other business relationships, including through contracts (...).”

OECD Due Diligence Companion (Draft), p. 3

“Tracking impacts by business relationships or working with business relationships to develop their own systems to track adverse RBC impacts and report them to the enterprise can be built into contracts, purchase orders, procurement requirements.”

OECD Due Diligence Guidance for Responsible Business Conduct (RBC) (Draft 2.1), p. 22

“(...) The company should: (...) Incorporate the supply chain policy set out in this Guidance into commercial contracts and/or written agreements with suppliers which can be applied and monitored.”

OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas, p. 74

“In order to induce factories to comply with upgrade and remediation requirements of the program, participating brands and retailers will negotiate commercial terms with their suppliers which ensure that it is financially feasible for the factories to maintain safe workplaces and comply with upgrade and remediation requirements [...].”

Accord on Fire and safety in Bangladesh (2018)

From Rana Plaza to Amazon: Questioning Contractual Practices

After the Rana Plaza disaster, which caused the death of over 1,100 workers, multinationals, whose products were manufactured in the Rana Plaza plant, explained that they had been victims of an uncontrolled subcontracting to the Rana Plaza workshops by their suppliers even though CSR clauses had been included in their contracts.

The disaster raised a question going far beyond the textile sector: Why do some direct suppliers or subcontractors, approved and bound by a CSR clause, take the risk to violate their contractual obligations?

“ It is important to remember that the Rana Plaza building had been audited just a few days before it collapsed, seriously calling into question the quality of audits that were provided for under CSR clauses.

Joseph Wilde-Ramsing, Senior Researcher at SOMO and Coordinator of OECD Watch

Lessons learned from the Rana Plaza disaster led to the publication of two documents pertaining to contractual practices:

- The Bangladesh Accord on Fire and Building Safety in Bangladesh signed on May 13, 2013 between 200 brands, sponsored and created by IndustriALL Global Union and UNI Global Union, in alliance with eight Bengali unions and NGOs.

“ By signing the Bangladesh Accord, the brands have committed to unprecedented contractual obligations consisting amongst others of: disclosing all their Ready-Made-Garment (RMG) suppliers in Bangladesh, ensuring that factories have the financial means to complete remediation with the terms of the Accord (article 22) and to maintain long term sourcing relationships (article 23).

Joris Oldzendiel, Coordinateur Bangladesh Accord

- French National Contact Point contribution toward the 2013 OECD guidelines, which then formed the basis for OECD Due Diligence Guidance for Responsible Supply Chains in the Garment and Footwear.

These documents highlight the weaknesses of some contractual practices between buyers and suppliers. Specifically, they noted a disconnect between customary contractual specifications, such as the objective, duration, price, compliance, delivery or penalties, and social requirements, including ethical commitments, compliance checks, whistle-blowing proceedings, etc. Because certain *business clauses* affect CSR clauses, special consideration should be given to contracts to avoid any imbalance. The graph below illustrates how the execution of a CSR clause is contingent on a number of other provisions stipulated in the contract and factors that must be considered when drafting it.



In addition, a CSR clause has to be reasonable to ensure its legal viability, as recently demonstrated by the Amazon example in France. The French Ministry of Economy and Finance filed a complaint against Amazon to the Paris Commercial Court or abusing its dominant position with some suppliers, claiming that the platform imposes unbalanced relations to its vendors. Under the complaint, the Economy Ministry is seeking a fine of Euro 10 million (\$11.8 million) against Amazon. This was a clear signal to companies that unbalanced contractual relations may subject them to sanctions.

This study shows that, in the light of the current regulatory requirements, commercial contracts, which stipulate that duty of care should be shared fairly between buyers and suppliers are crucial in business relations.

“ Contractually shift all the duty of diligence on suppliers becomes a factor of legal risk for buyers.

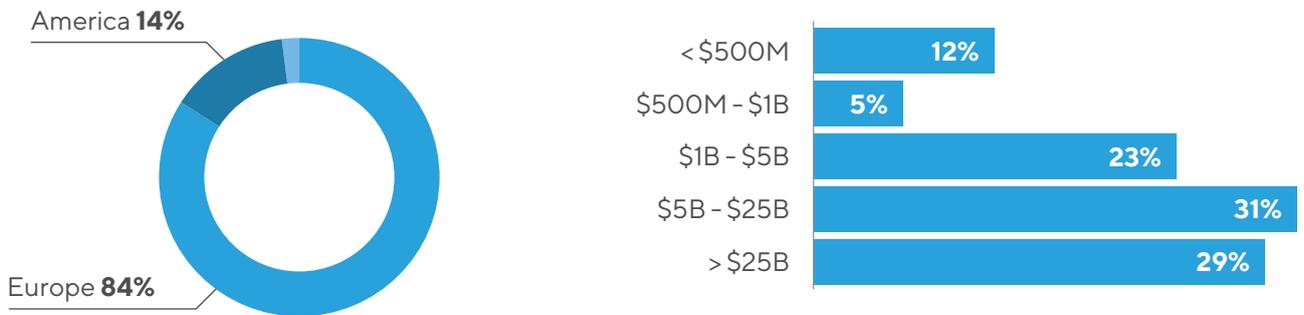
Peter Herbel, Partner at Herbel Avocats, former Legal Director, Total Group

Methodology

The study is based on two surveys conducted among members of the key participants in most global business transactions buyers, who are typically the organizations enforcing a CSR clause, and suppliers, who receive CSR instructions. In total, 50 buying organizations described their contractual practices pertaining to sustainability and 519 suppliers commented on their experience with codes of conduct and CSR obligations. The most interesting answers were followed by in-depth interviews aimed to gather examples of best practices and valuable experiences.

The study provides an unbiased overview of both, buyers' and suppliers' interests, even if they are conflicting. It stipulates that commercial contracts should include social and environmental requirements in a way that is effective and without putting suppliers at a disadvantage.

Respondent Profiles: Buyers



Respondent Profile: Suppliers



A CSR Clause: Placement in a Contract and Key Characteristics

Given the increasing transparency demands around the world, a growing number of contracts now reference environmental, social and governance issues, combining implications offered by soft law and hard law. These references take on the form of a so-called CSR or sustainability clause, which may prove an effective way to guarantee compliance from suppliers from tier-1 through the entire value chain, even those operating in countries with improved governance.

General Figures



of companies include a sustainability clause in their procurement contracts*



of companies monitor the environmental and social performance of their suppliers*



of companies are not sure if they are able to terminate their contract in case of CSR violation*

*Figures provided by the International Association of Contract and Commercial Managers (IACCM)

The fact that a large proportion of businesses include a sustainability clause in their procurement agreements shows that CSR is becoming a significant part of contract strategy. However, due to operational and legal obstacles, many of those clauses remain in the infancy stage.

CSR Clause Features

The study has identified four key features of a CSR clause, which retain relevance regardless of the legal system the contract is drawn in. These four features can be seen as essential building blocks for a sustainability clause and for this reason have been used in a diagnostic tool, which has been developed to describe different levels of practice:



Components	Maturity Criteria
1. Reference to ESG standards	Precision
2. Obligation of assessment or certification	Verifiability
3. Consequences in case of breach	Enforceability
4. Tier-n reach	Coverage Depth

1. Reference to ESG Standards

Observations

Apart from stating that the supplier must abide by the relevant law, CSR clauses refer to two types of instruments: internal standards (code of conduct, policy, ethical charter) and external instruments (Global Compact, ILO conventions, OECD guidelines, ISO 26000, etc.). This integration of non-contractual standards into the contract gives them a binding force.

Implications

This first component of a CSR clause defines its scope. The primary contracting party, typically a buyer, states what issues are important in a given business relationship. They often set requirements that are very generic and can undermine the operational effectiveness and the binding force of a CSR clause.

	BASIC	PROGRESSING	ADVANCED
Precision	General principles	Policies expected	Objectives settled

Survey Results

The survey shows that an overwhelming majority (over 75 percent) of clauses express general principles and less than 5 percent set precise objectives.

2. Verifiability

Observations

A key advantage of a well-written CSR clause is that it makes it possible to verify whether sustainability obligations are being fulfilled. The assessment provision makes it mandatory for a supplier to be evaluated on its CSR performance.

Implications

Rather than only referencing standards, an obligation to be assessed constitutes an “obligation of result” and not an “obligation of means,” as defined by Demagogue, a French legal scholar. As a result, a supplier cannot refuse an audit by the customer or a third party. However, a number of operational elements must be considered with regard to this kind of clause such as ensuring that audits are unannounced, deciding on their frequency or who covers the cost of the assessment. These elements may be defined in an annex to the contract.

	BASIC	PROGRESSING	ADVANCED
Verifiability	None or supplier self-assessment	Third-party assessments	Third-party assessments conducted regularly

Survey Results

The survey shows that companies have fully understood the necessity to regularly assess their suppliers. However, there are large differences in how mature they are in this approach. Only 25 percent of CSR clauses stipulate that costs are to be shared between buyers and suppliers, with the rest charging the suppliers for all the costs associated with the assessments.

3. Enforceability

Observations

Most of the clauses reviewed for the purpose of this study define consequences of breaching the CSR clause. This defined liability regime affords buyers more certainty and reinforces, in the eyes of suppliers, the fact that the CSR clause is an essential part of the contract, just like any other commercial clause.

Implications

The effectiveness of this enforceability is contingent on a number of factors, including the question of whether or not a reasonable share of responsibility lies with the supplier. If this is not the case, the clause can be deemed unenforceable.

	BASIC	PROGRESSING	ADVANCED
Enforceability	No consequences defined in case of breach	Possible penalties in case of breach	Progressive steps to follow in case of breach

Survey Results

As much as 75 percent of clauses specify that a violation of the CSR clause can be a cause for an early termination, but only 12 percent have actually resorted to termination.

4. Coverage Depth

Observations

CSR clauses under review include obligations regarding sub-suppliers, subcontractors and subsidiaries. However, they are not always sufficiently specific and sometimes state only that CSR principles shall be guaranteed through the supply chain.

Implications

Extending CSR clause enforceability beyond the direct business relationship raises operational and legal difficulties, regardless of the law applicable to the contract.

	BASIC	PROGRESSING	ADVANCED
Coverage Depth	Partial coverage of tier-1 suppliers	All high-risk tier-1 suppliers	Beyond tier-1

Survey Results

Most of CSR clauses state that the tier-1 supplier must include similar requirements in their own procurement contracts, which guarantees penetration down to tier-2.

Operational and legal complexities related to CSR clauses as well as areas for improvement for each of the fundamental clause components will be discussed further in this paper.



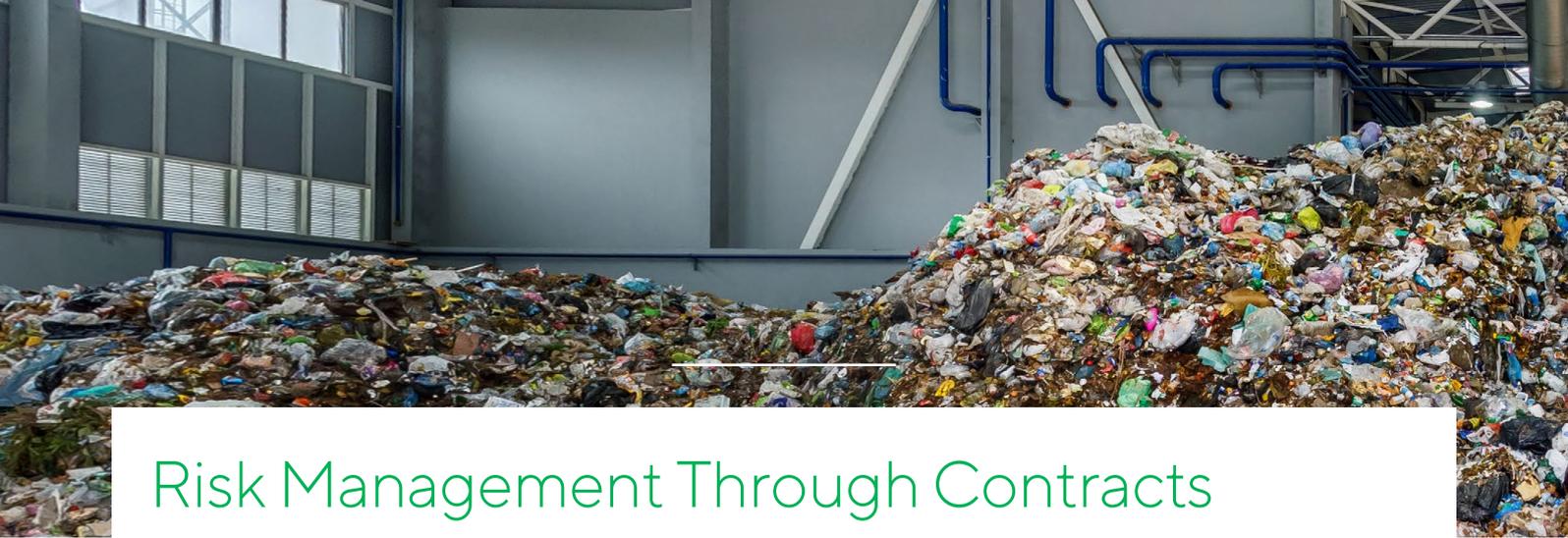


Risk Management Through Contracts

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Risk Management Through Contracts

When asked about the main reasons for integrating a CSR clause, 49 percent of companies responded that they wanted to mitigate social and environmental impact in their supply chain and 31 percent sought protection against legal proceedings. However, eliciting a clear answer on how to measure the effectiveness of a CSR clause was much harder.

It is also noteworthy that the search for legal protection raises the question of CSR clause coverage. For contractual protection to be effective, three requirements have to be met: the clause must cover all relevant issues, it must be included in all risky contracts and address the risk further down in the supply chain.

Survey Results: The Scope of a CSR Clause

Sustainability Issues

Most of the CSR clauses reviewed cover the main areas of CSR diligence, which shows awareness of CSR issues. However, as it is impossible to treat all those issues with the same level of attention, it appears that CSR considerations are only limited to a compliance exercise.

To ensure a CSR clause is effective it has to be defined by a number of parameters specified in the contract, such as the country, sector, supplier size, etc., outlining how it applies to the given transaction.

BUYERS

What aspects are listed in your CSR clause?





“ The choice of CSR issues can be justified according to a risk evaluation. The level of ESG due diligence shall be proportionate to the risk of human rights violation.

Katia Martin-Chenut, Researcher at CNRS/Université Paris 1 Panthéon-Sorbonne, member of the French National Consultative Commission for Human Rights

“ Companies must avoid catch-all clauses that cover issues ranging from corruption to human rights. These provisions have to be considered one by one.

OECD Debates, Forum on Due Diligence in the Garment and Footwear Industry (January 2018)

Lack of precision is a risk factor

The study revealed that CSR clauses, as well as charters or codes of conduct that accompany them, are often too generic.

Lack of precision may be risky for buyers in two ways: 1) the buying organization cannot expect complete liability release in the event of damage and 2) the supplier can legitimately expect an adaptation of the conditions. In addition, a number of possible interpretations lead to legal uncertainty. (All these sources for interpretation conflicts and by consequence legal uncertainty.)

“ Under German law, CSR clauses can be deemed invalid if they are not properly drafted. A clause which confines itself to referring to general CSR principles is often too vague to be enforceable.

Birgit Spiesshofer, Attorney at Law, Chair of the CSR Committee of the Council of Bars and Law Societies of Europe (CCBE)

“ The new French civil code endorses the theory of legitimate expectations, objectively appreciated for every type of contract (sales, services...). This reference to the quality “conformed to the legitimate expectations of parties” reveals the importance of the expectations of the person that you commit to. In the future, this can become an instrument of creation and transmission of obligations whose standards will have been defined by practice and soft law. For instance, in CSR, the lack of efficiency of companies commitments is widely denounced. This new concept could contribute to make them binding, by taking into account the general rise of expectation in this field.

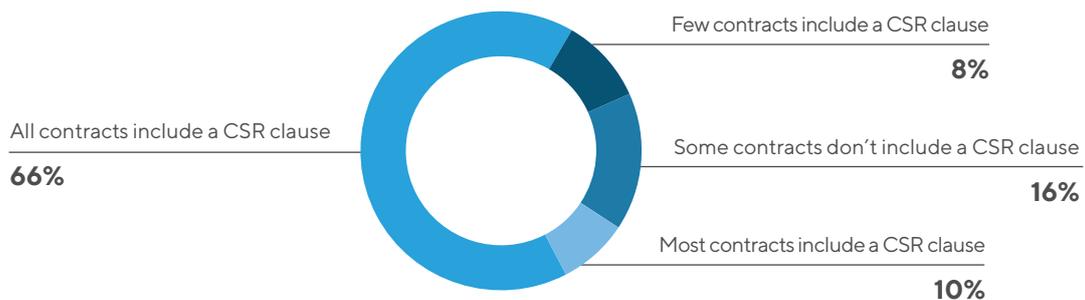
Bénédicte Fauvarque-Cosson, Attorney at Law, Chair of the CSR Committee of the Council of Bars and Law Societies of Europe (CCBE)

Supplier Risk Mapping

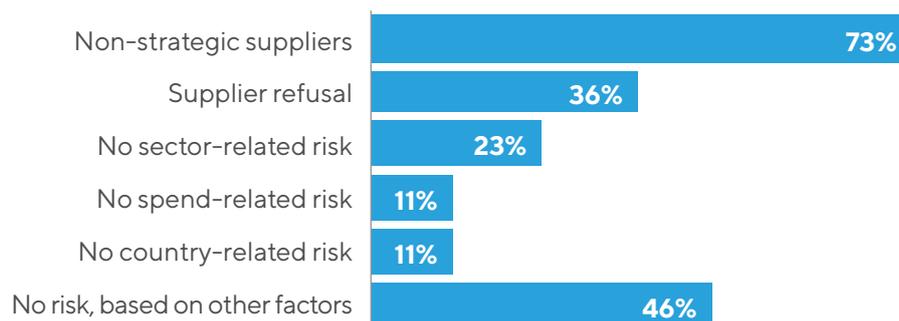
Most companies systematically include a CSR clause in their contracts, but there are some who decide to proceed through a risk analysis, taking into account various aspects: sector, spend, country. Occasionally, buyers choose not to include a sustainability clause if this has been requested by suppliers (this practice is discussed in more detail under “Negotiation”).

BUYERS

Do you typically include a CSR clause in your contracts with suppliers?



What are the reasons not to include a CSR clause?



🏢 SUPPLIERS:

Have you ever been asked to sign a CSR clause?



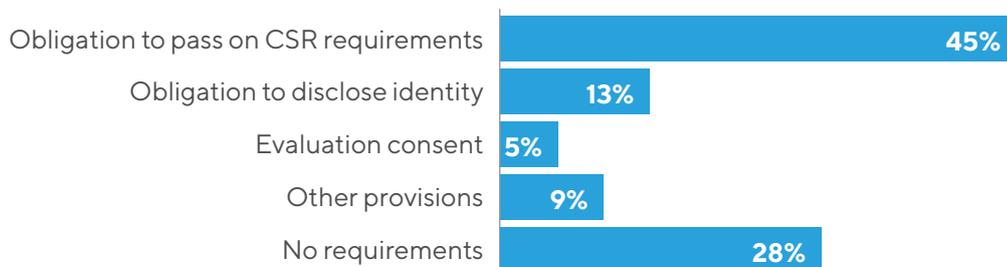
These contractual requirements are based on a first step of risk mapping, i.e. identifying the most risky points in the supply chain, which helps prioritize actions. Even if the optimal objective is to include a CSR clause in every contract, risk mapping should be conducted to guide the process and, in the first place, include it in the highest risk contracts.

Supply Chain Coverage

To ensure coverage further down the supply chain, 75 percent of CSR clauses contain requirements regarding tier-2 suppliers and beyond. These requirements may appear in a number of forms, using different legal mechanisms.

🏢 BUYERS

Does your CSR clause include requirements regarding your tier-2 suppliers?



🏢 SUPPLIERS

Do your customers include requirements regarding your tier-2 suppliers?



The survey identified three forms of requirements regarding tier-2 suppliers: obligating the supplier to include similar standards in their own contracts (included in 45 percent of clauses), obligating the supplier to declare the names of all sub-suppliers implied in the supply chain (35 percent) and allow assessments of the sub-suppliers (5%).

“ We require our suppliers to relay our values to their own suppliers, but not necessarily our code of conduct. It is better to stay flexible because signing a code of conduct by a remote organization may not be perceived well. In addition, it implies a huge legal burden on suppliers. ”

— A comment from in an in-depth interview with a buyer.

Another solution is to exert control on the procurement system of the direct supplier. If there is an effective management of sustainable procurement, the risk is automatically decreased for the entire supply chain. As noted above, 73.4 percent of CSR clauses cover sustainable procurement.

⚠️ A strictly conditioned delegation of responsibility

One of the objectives while taking tier-2 suppliers into account is to delegate responsibility in case of ESG violation. The scope of the legal efficiency and validity of this delegation must be outlined. Under no circumstances can the buying organizations expect an absolute exoneration of liability.

“ A clause which directly implements the wide responsibility conception of the UN Guiding Principles for “directly linked” third parties may be void as it may contradict the fault-based liability conception of German law. ”

— **Birgit Spiesshofer**, Attorney at Law, Chair of the CSR Committee of the Council of Bars and Law Societies of Europe (CCBE)

“ There are already legal ways to hold the buyer responsible if they do not put their suppliers in the right conditions to be diligent for their own business relations. ”

— **Muriel Fabre-Magnan**, University of Paris 1 Panthéon-Sorbonne

Toward a Shared Responsibility Along the Entire Supply Chain

It is noteworthy that even if for a large majority of organizations interviewed during the study involving tier-2 is limited to asking tier-1 suppliers to relay CSR requirements on to their suppliers, they typically know who their tier-2 suppliers are and are familiar with their CSR performance. This information makes it possible for businesses to respond to the growing demand for product tracking in complex supply chains. These practices illustrate the progressive transition from the “Know your supplier” principle to “Know your supply chain”.

“ We would note that this is typically a trickle-down effect. For example, we have seen these broader CSR and sustainability contract clauses imposed by large multinationals in their standard form contracts, especially where those multinationals have material voluntary CSR and sustainability commitments that they are looking to pass down their supply chain. This in turn results in the contracting party looking to pass on similar obligations with its own supply chain.

Paul Davies and Sophie Lamb, Partners at Latham & Watkins, London

Regardless of the way ethical commitments are conveyed from supplier to supplier, the fact that it happens means that responsibility is allocated along the entire supply chain. This trickle-down effect leads to an operational and judicial difficulty for the organization: how do we ensure that every link of the chain can fulfil its responsibility?

“ These business relationships that are more and more nourished of ESG demands progressively establish a shared responsibility from different parts linked to the contractual chain.

Mustapha Mekki, University of Paris 13, Sorbonne-Cité



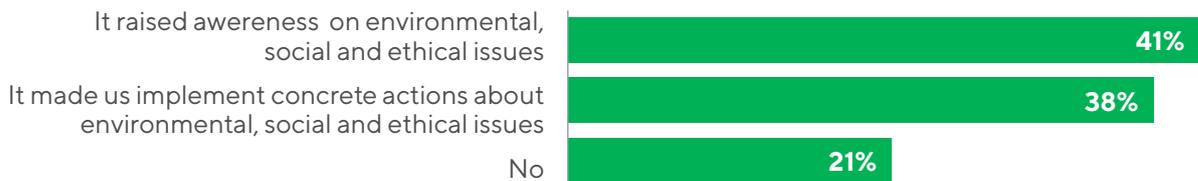
A Positive Impact on Suppliers' CSR Practices

Survey Results: CSR Clauses Positively Impact Suppliers Practices

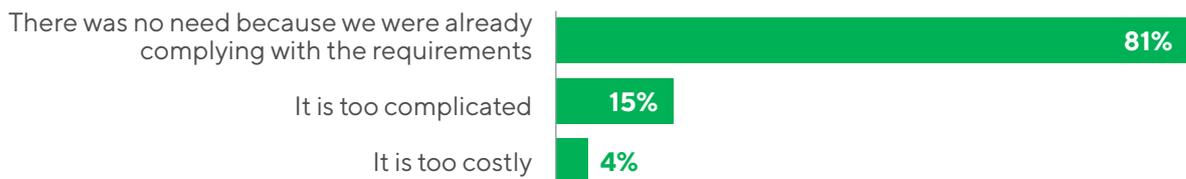
The supplier survey revealed that contractual obligations related to CSR impact their sustainability practices.

SUPPLIERS

Have your CSR contractual obligations made you change in any way your business practices?



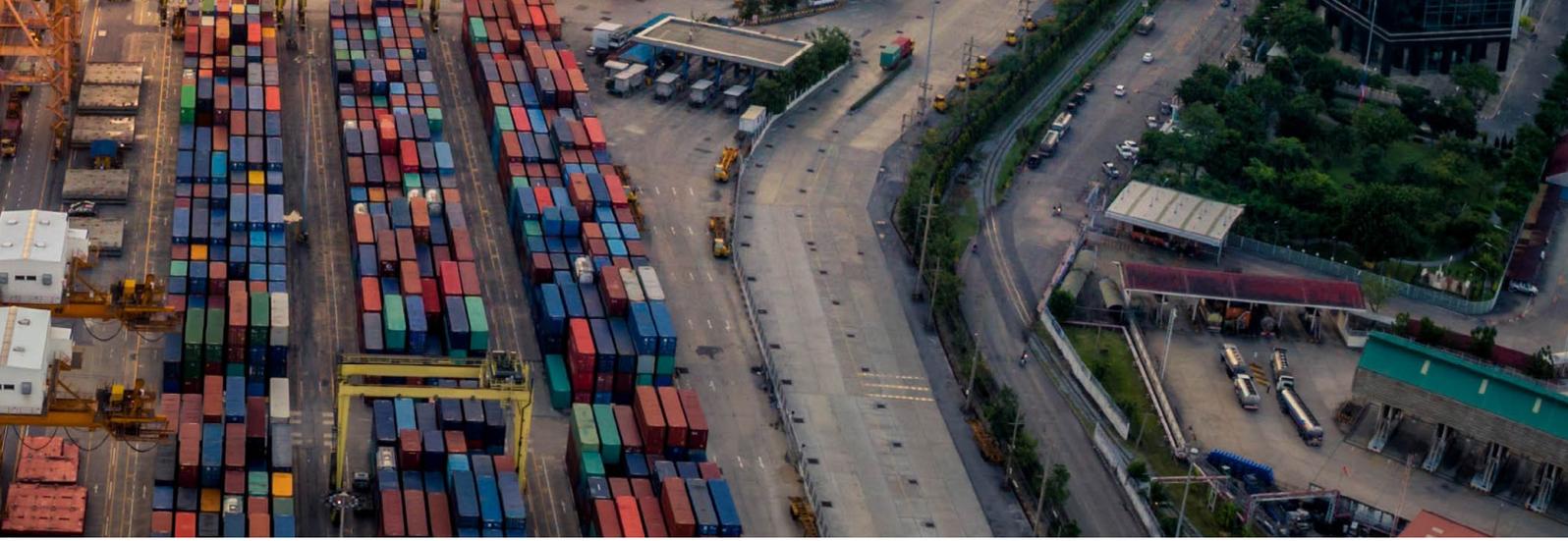
If not, why?



For 79 percent of suppliers, having CSR requirements in their contracts had a positive effect on them, whether it raised awareness (41 percent) or made them implement concrete actions (38 percent). A lot of them learnt the notion of CSR through contract negotiations. Facing the same requirement from a number of customers has led to changes in supplier practices, even if it is unclear whether these changes were triggered by principles or business purposes.

“ CSR clauses object should be to guarantee the respect of norms to ensure both health and safety of suppliers workers and safety of product for the consumer.

Peter Herbel, Partner at Herbel Avocats, former Legal Director, Total Group



“ We work with a number of global brands that have made specific demands regarding CSR compliance in line with their published policies on sustainability, ethics and the environment. This has driven our business to implement processes and ways of working to support compliance across our operations. This has been a journey where we have collaborated with our clients and suppliers in order to improve.

A comment extracted from the supplier survey

The suppliers who said a CSR clause in the contract with their customer had not resulted in any changes in their practices – mostly those based in Europe and North America – had already various CSR policies in place. As many as 81 percent of them stated they did not need to do anything as they were already compliant.

“ When enterprises respect human rights in their activities and in their supply chain, they produce a high scale, unprecedented positive impact on the lives of persons that need advantages from sustainable development the most.

John Ruggie, former UN Secretary-General’s Special Representative for Business and Human Rights

Key Points to Remember

✓ **Risk mapping**

Essential to answer to the growing demand of product tracking, there is a progressive transition from “Know your supplier” to “Know your supply chain.

✓ **Setting achievable objectives for suppliers**

Whether a CSR clause will be effective depends largely on how reasonable are its requirements.





Ensuring Successful Implementation

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Introduction

There are both legislative and operation challenges related to CSR clauses, such as ensuring the efficiency of supplier assessments or legal certainty that a contract will be terminated in the event of the CSR clause violation.

The study shows that CSR clauses still need to find their place among other contractual provisions. Establishing a CSR clause within a commercial contract in a way that ensures compliance and compatibility with all the business aspects is a major challenge in moving from sustainability clauses to sustainable contracts.

“*In the analysis of due diligence measures implemented by companies of the footwear and garment sector in the framework of the “Rana Plaza report”, we pay a special attention to the contract terms and conditions dedicated to CSR. It even led to the first of the 10 recommendations of the French National Point of Contact: “Include ethical commitments and respect of norms into contracts.*”

Maylis Souque, General Secretary at the French National Point of Contact of the OECD

Exercising Influence

The study shows how the contractual efficiency of a CSR clause depends on a number of complex factors, including the extent to which customers are able to influence the other party in business relationships. This aspect, which is stipulated by the OECD and UN guiding principles, is critical throughout the entire duration of the contract and before:

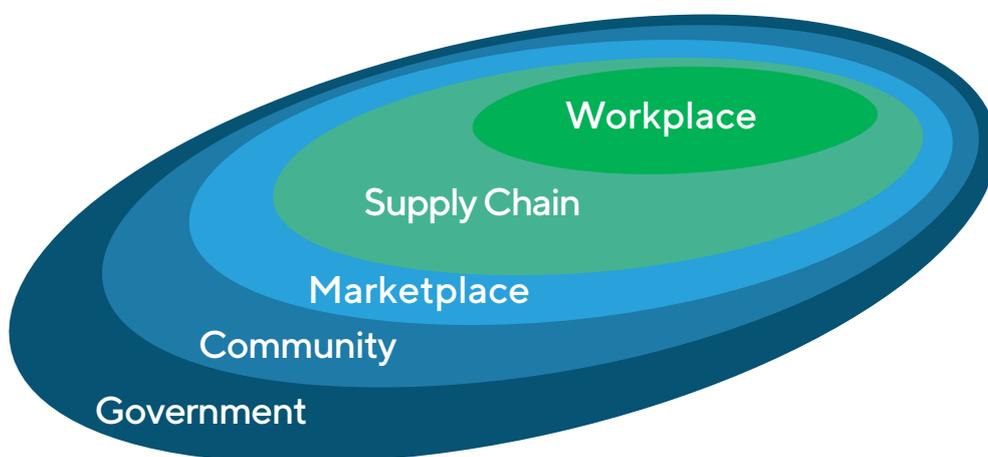
- During **negotiations** – to ensure is the clause is properly incorporated in the contract;
- During **assessment** – to check if/how it is implemented;
- Over the course of **the entire cooperation** to promote a favorable environment to meet CSR objectives;
- In the **event of a breach of the clause** – to lead to the **termination** of the contract.



Meanwhile, ISO 26 000 defines the sphere of influence within which companies must embrace these principles as: “a scope/extent of political, contractual, economic or other relationships through which an organization has the ability to influence the decisions or activities of individuals or other organizations.”

This shows the variety of parameters that need to be taken into account. The volume of purchase, the history of the relationship, the size of the supplier, its position in the value chain or the quality of the governance of the country of supply are likely to have an impact on the primary contracting party’s level of influence.

Sphere of influence (source: Office of the United Nations High Commissioner for Human Rights)





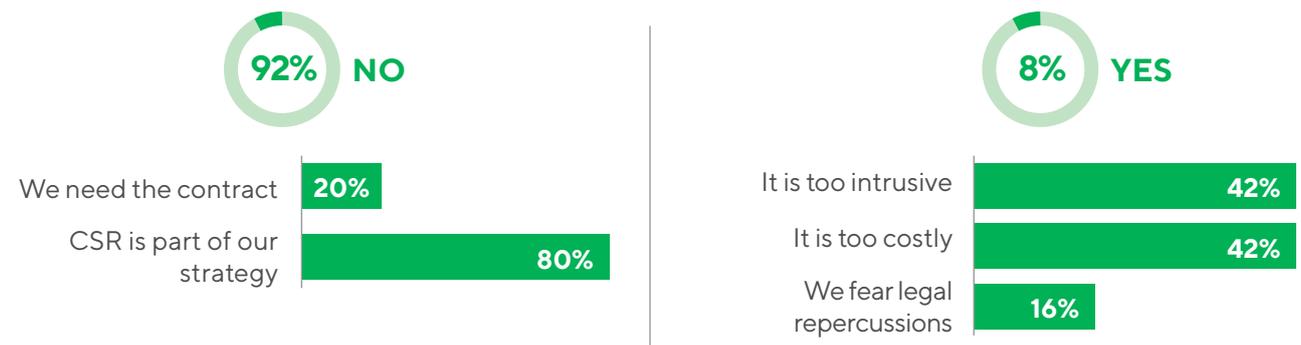
From Effective Negotiations to Effective Endorsement

Survey Results: CSR Clause Adoption Around the World

Effective negotiations are key in ensuring that a CSR clause is included in the contract. They guarantee supplier engagement and effective due diligence.

SUPPLIERS

Have you refused to sign a contract because it included a CSR clause? Why?



CSR clauses are generally accepted around the world: only 8 percent of suppliers said they had decided not to sign a contract because it included a CSR clause. The main reason behind it was the cost related to CSR compliance and perceived interference with the suppliers' management.

It is also noteworthy that among the 92 percent of suppliers accepting a CSR clause, as many as 80 percent do so willingly, while the remaining 20 percent feel they have no other option; in other words they agree to CSR commitments to make sure they do not lose the contract.

SUPPLIERS

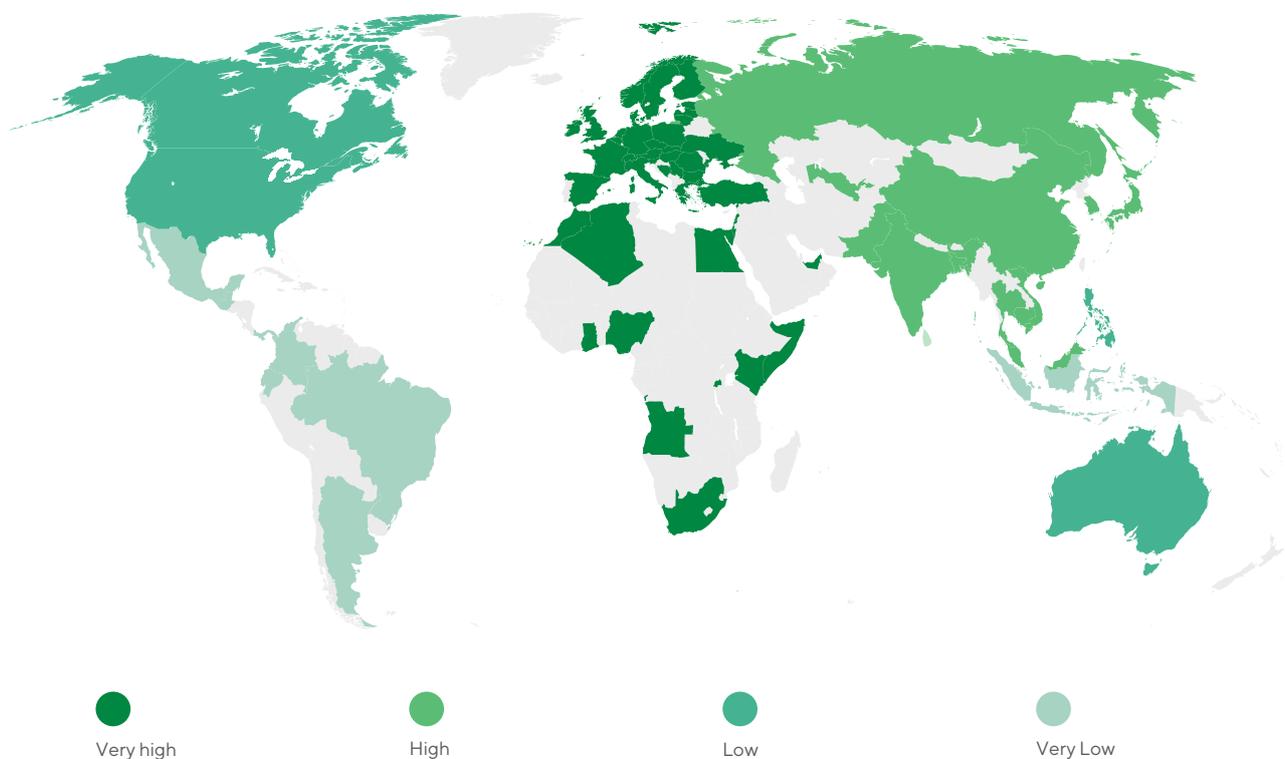
How do you generally perceive the CSR requirements?



It must also be noted, however, that the 80 percent of suppliers who find CSR requirements reasonable are mostly located in Europe and North America, as they comprised the lion's share of the sample. These are countries with mature CSR legislations, which results in a better understanding of CSR demands.

The study also identified key reasons why suppliers refuse to sign contracts that include a CSR clause and grouped them by geographical regions. An Acceptance Index based on the positive and negative responses shows that CSR critics are largely located in the Americas, with the rest of the world generally accepting CSR clauses.

Geographical distinctions: CSR adoption over the world (index from 1 to 10)



Looking at the Americas, satisfaction levels are comparable in North and South America, however, the reasons for CSR clause criticism are completely different. Asked about their perception of CSR demands, 26 percent of North American suppliers said they were out of touch with these activities, compared with only 14 percent of European suppliers and the average of 19 percent. The evidence gathered during the study suggests that there is a general feeling among North American suppliers that CSR clauses are designed for and apply only to high-risk sectors and countries.

In Latin America, meanwhile, a significant part of suppliers said the main reason why they were reluctant to sign a contract including a CSR clause was lack of internal resources and expertise (34 percent). However, only 8.6 percent of the suppliers said the main reason why they did not want to enter into such contracts was the level of production expected. This is in contrast to Europe and Asia, where 33 percent of suppliers said they have means dedicated to CSR but struggle to combine these requirements with the other objectives.

These geographical differences are clearly linked to the extent to which CSR is understood and acknowledged in different countries. In Europe and Asia the understanding of CSR principles is no longer an issue, however, there are still difficulties related to their implementation.

Recommendations: Discuss, Negotiate and Provide Training

All critical comments expressed by suppliers have one thing in common: they suggest there is a lack of dialog between contracting parties regarding the placement of CSR in their contractual relations. At the same time, however, the study shows that suppliers are willing to negotiate the inclusion of a CSR clause, which suggests they do understand the changing requirements and are ready to work to identify solutions.

“*If a company is able to determine its minimum requirements and demonstrate flexibility in how its objectives are achieved, it is more likely to have success in influencing its supply chain and the behavior of the parties it contracts with.*

Paul Davies and Sophie Lamb, Partners at Latham & Watkins, London

We are therefore left with the challenge to create the right conditions for this kind of dialog. These conditions could be built upon **buyer training** on how to **negotiate with suppliers who are unwilling to enter into a contract including a CSR clause**.

Buyer Training

Including a standard CSR clause in a commercial contract may appear to be a sensible option at first, however, the study shows this practice has its drawbacks: It limits the extent to which the contracting parties are involved in the process and may reduce the binding force of the clause.

““ *Our buyers are trained to communicate with suppliers. We do not want it to be a matter of “ticking the box”.*

Marleen Van Mensel, Senior Lawyer, Solvay

““ *Reputation is a critical corporate asset and Procurement is in the front line for its protection. Developing skills and knowledge in the field of CSR is no longer an option - it is core to the Procurement training agenda.*

Tim Cummins, President of the International Association for Contract & Commercial Management

Companies should work to raise awareness and train procurement professionals on sustainable purchasing to ensure their understanding of social criteria, and not just the price and quality of the products.

““ *You can tell the difference from a trained buyer to one that is not. It is painful, for us and for them. They cannot negotiate, because they were told “put this clause in all the contracts” without understanding why.*

A comment from an in-depth interview

This kind of training should include aspects of legal and reputational risk and equip buyers with skills for effective negotiations. Rather than refuse any changes or modifications to the CSR clause they need to be able to respond appropriately to the concerns expressed by suppliers.

Negotiation Table

The table below lists the main reasons why suppliers refuse to sign a contract including a CSR clause, as identified by the study, along with suggested solutions. The solutions are explained in more detail below.

Reason for refusal t	Solution	Section
<p>Irrelevance The CSR clause has not been adapted to the context of the transaction.</p>	<p>Adapt the clause to the supplier Buyers need to make case-by-case adjustments to the CSR clause.</p>	<p>Ensuring Diligence Through Clause Customization P.35</p>
<p>Intrusion The option of assessment perceived as too intrusive.</p>	<p>Be specific about assessments Buyers need to be able to clearly communicate the benefits of CSR compliance and assessment.</p>	<p>From Adequate Evaluations to Efficient Follow-Up P.43</p>
<p>Enforceability Penalties listed as consequences of a breach perceived as a deterrent.</p>	<p>Fair share of responsibilities, progressive penalties system Suppliers must not bear too much of a responsibility burden, which can be helped by the introduction of a progressive penalties system.</p>	<p>Cooperation Between Buyers and Suppliers as the Key to Effective Implementation P.48</p>
<p>Cost The cost of compliance with the CSR clause requirements perceived as too high.</p>	<p>Incentives, share costs Rewards and assistance from the buyer helps mitigate the financial burden and demonstrates true commitment to CSR issues.</p>	<p>Cooperation Between Buyers and Suppliers as the Key to Effective Implementation P.48</p>

Lack of negotiations may result in an unenforceable contract

It is noteworthy that in commercial law there are essentially six elements that must be present for a contract to be enforceable. There must be an offer, acceptance of the offer, consideration, capacity, mutuality and the terms and conditions must be legal and not in violation of any laws or ordinances. Lack of negotiations before the contract is signed, including negotiations regarding the CSR clause, may be linked to lack of consideration or lack of mutuality and, as a result, deem the clause invalid and the contract unenforceable. Therefore, the drafting of a customized CSR clause must be preceded by negotiations.

“ *Contract terms which have not been individually negotiated may be invoked against a party who did not know of them only if the party invoking them took reasonable steps to bring them to the other party’s attention before or when the contract was concluded.*

European Principles of Contract law, Article 2:104: Terms Not Individually Negotiated

“ *The risk of a CSR clause that is not negotiated is the one inherent in adhesion contracts: a discrepancy in the contractual relationship.*

Mustapha Mekki, University of Paris 13, Sorbonne-Cité

Ensuring Diligence Through Customization

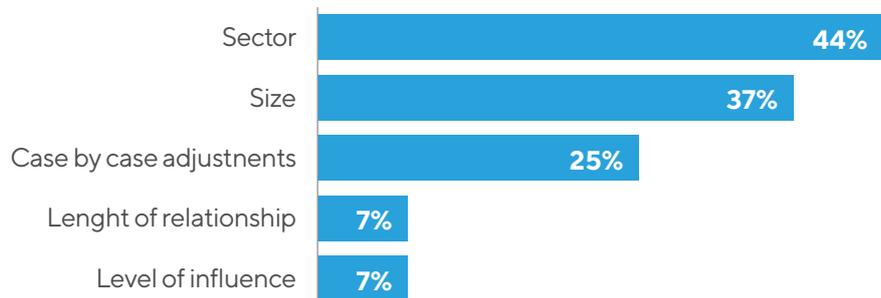
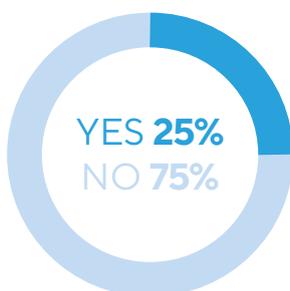
Survey Results: Standard Clauses Disconnected From the Context

Clauses Are Rarely Adapted

Only 25 percent of the companies interviewed during the study said they adapt their clause to their suppliers, and this adaptation being mostly based on the supplier size (37 percent) and sector (44 percent). A quarter out of these 25 percent do not have customized clauses but accept case-by-case adjustments when faced with a collaborative approach from the supplier.

BUYERS

Do you adapt your clause to your supplier?



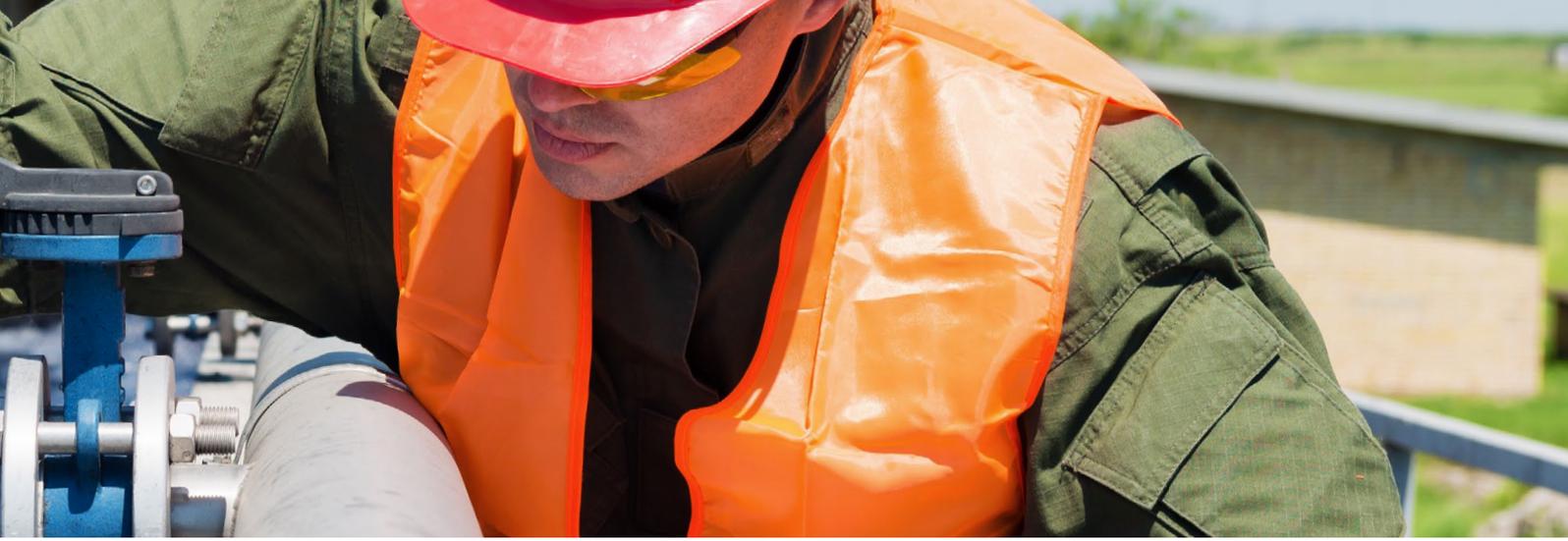
Clauses Are Seen as Irrelevant

This standardization may result in the poor reception of CSR requirements by suppliers. As stated above, 18 percent of suppliers perceive the CSR commitments as irrelevant and a lot of comments point out the absurdities resulting from this problem.

“Many big customers push general demands to their supply chain. We are a software development company, so requirements about third world countries mining industry have no relevance.”

It happened several times that we were underrated because the demands were not applicable to our industry. For instance, once a large portion of the score was based on sustainable product design. Because we don't design products, our score was low.

Comments from the supplier survey



CSR Clauses Are Not Read

An attempt to cover all risks from all kinds of suppliers leads companies to adopt very broad CSR terms and conditions, which results in lengthy codes of conduct. This has a major impact: they are not read. As many as **100 percent of the suppliers we had in-depth conversations with stated that they do not read codes of conduct** from all their customers because the process is too time-consuming.

“ Customers require every employee entrusted with dealing with their orders to know their CSR requirements often comprising 40 pages. It is not feasible in a medium-sized company to have employees read and comply with so much detail, particularly when the company has several such customers.”

For the most part, we have stopped reading each customer’s individual CSR documents/requirements [...]. The amount of time necessary to read and assess lengthy, customer-specific requirements is negatively impacting our internal resources, increasing costs, extending lead times (for contract review), and decreasing our customer service response time.

Comments from the supplier survey

Recommendations: Contextualize the Clause

All CSR clauses may share the same core statements, intentions and obligations based on the general international CSR guidelines and commitments. However, having only a “catch-all” clause will negatively impact due diligence mechanisms and result in violation risks. To ensure effective due diligence, companies must adapt their contractual demands and justify them. In doing so they may prioritize CSR risks which require particular attention.

Adapting to Resources

Forcing non-customized CSR demands onto small- and medium-sized companies typically results in disproportionate obligations with regard to their size, such as forming committees or dedicating a full-time position to CSR duties, and this may result in poorer engagement.

 *As a small business manufacturing commercial components in the USA, we are committed to ethical and responsible conduct, but we do not have the internal resources to review and react to all of the overreaching and often not-applicable language and documentation requirements being flowed to us from a very diverse, international customer base.*

 *It happens often to have one week to respond to a tender and a 40 pages long code of conduct to sign. No one has the time to read this, even less a busy seller. We are a small company, the requirements applying to us could be contained in 4 pages.*

Comments from the supplier survey an in-depth interview

Therefore, when drafting or negotiating a CSR clause, buyers should consider suppliers' human and financial resources. To ensure effectiveness of the clause these adaptations should also consider the size of the suppliers and their needs. In addition, as indicated by the suppliers, CSR clauses should be more concise and should avoid listing any irrelevant demands.

Adapting to Sector

 *The reasonable character of demands on the supplier will be measured with regard to its adaptation to the context of activity.*

Jean-Claude Javillier, Professor and former Director of International Labour Standards Department, ILO

CSR risks vary considerably from sector to sector. This is why taking these differences into account enables helps ensure effective diligence.

 *The margins of logistics companies are very small, but the expectations are the same as for manufacturers. While I understand the importance of these codes, some contain requirements that do not apply to us in the same way they apply to manufacturers. More codes of conducts need to consider industries in their demands. A cookie cutter approach, while efficient, is not effective in all cases.*

We must move from pure checklists to consideration of material activities and individual programs.

Comments from the supplier survey

To do so, it is vital to first identify risks associated with the purchase categories, which requires considerable documentation work. This risk map must be updated regularly, taking into account sector initiatives, new sector-specific regulations and relevant government and non-government reports.

“ Our reports on the human rights impacts of some sectors are meant to catch the attention of large buying companies. We are attentive to the adaptation of their procurement strategy.

Joseph Wilde-Ramsing, Senior Researcher at SOMO and coordinator of the OECD Watch

Adapting to Country

“ Targeting some countries in priority for human rights issues can justify a greater allocation of resources.

Kathia Martin-Chenut, Researcher at CNRS/Université Paris 1 Panthéon-Sorbonne, member of the French National Consultative Commission for Human rights

We can identify two types of situations: countries with regulations that are in line with international standards and those whose regulations or governance require greater contractual vigilance and precision when prioritizing CSR risks.

“  Here and in our other sites many CSR clauses are already legally followed. Child labor as an example is strictly regulated, and workers are free to join any unions. We need to have equality guidelines and people know their rights, so I feel some of the clauses more self-evident than as a real guideline.

A comment extracted from the supplier survey

Adapting to the Position in the Supply Chain

“ Determining the position of the supply chain and the proximity with major ESG risks allow to adapt the clause accordingly.

Joseph Wilde-Ramsing, Senior Researcher at SOMO and Coordinator of the OECD Watch

CSR clauses may also be adapted depending on the position of the contracting parties in the supply chain. Some companies intervene at a *pinch point*, where they have a degree of influence and visibility to the other actors. These are generally key transformation points in the supply chain, or steps where just few actors may transform the majority of the product, or where the visibility into the production and the commercialization of the product is broad. At the stage of *pinch points*, the relatively low number of actors increases the impact of any change in the practice.

An example issued from the ILO-IOE Guidance Tool for Businesses on Child Labor in the Cane Industry:



The study of the sugarcane supply chain shows a *pinch point* at the level of mills that collect and transform raw material. These actors are in close contact with child labor issues, which enables them to obtain valuable information and exercise their influence. Companies down the sugarcane value chain must pay particular attention to this stage of the chain and establish a direct dialogue with the mills, where possible, or by joining initiatives, which are likely to have a positive impact on them.

“ Devising workable approaches to child labour impacts that are far removed from the company’s own operations entails understanding how the value chain operates, the root causes that lead to the use of child labour at relevant points in the chain, and where in the chain a company’s leverage may be the greatest, either alone or in collaboration with other actors.

ILO-IOE child labour guidance tool for business, p. 43

The concept of a *pinching point* applies to any supply chain. The actor must consider its position and its supplier’s in the supply chain in order to adapt the clause. While it would be difficult to develop this kind of diagnostic for each procurement situation, it is possible to draw up supplier profiles, e.g. producers, cooperative, trader, and create a clause template for each of those profiles. The contractual details that this template would impact are the level of detail of the information required for the lower tiers of the supply chain, whistleblowing mechanisms, engagement of local stakeholders, etc.

Future Considerations

	BASIC	PROGRESSING	ADVANCED	FUTURE CONSIDERATIONS
Contextualization	None	By size / sector / country	+According to risk mapping / analysis	Individual ESG improvement plan

✓ **Develop a CSR clause guide available to buyers**

The guide would outline general principles, key definitions, assessment procedures, etc.

✓ **Develop an individual CSR priority schedule with suppliers**

Essential to measure the follow-up of performances according to the context of the contract.





From Adequate Evaluations to Efficient Follow-Up

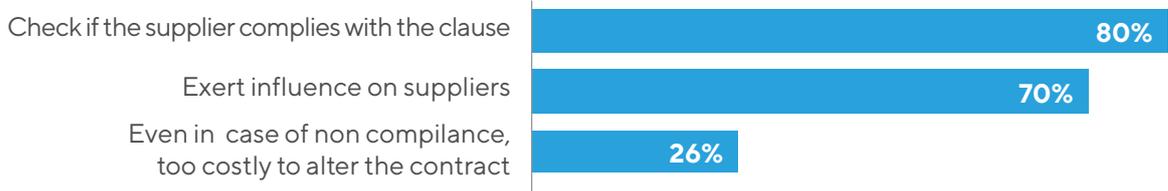
Survey Results: Risks Associated With Strict Compliance

A Challenge for Buyers

The study found that the biggest challenge for as many as 89 percent of buyers is to ensure that the CSR clause is respected, followed by the ability to influence suppliers.

BUYERS

What is the main challenge regarding CSR clauses?

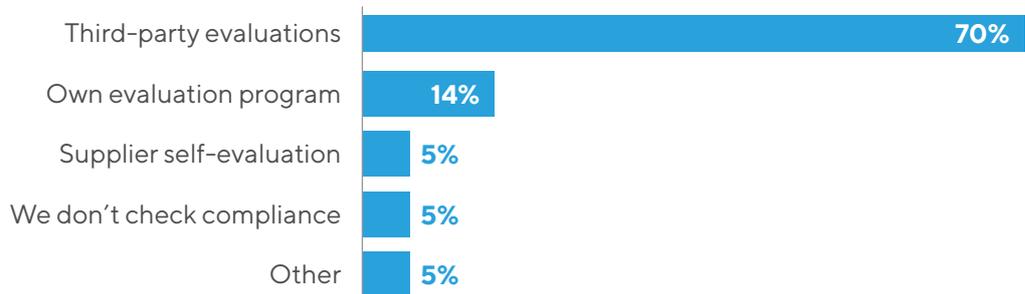


Assessing CSR compliance is hard given the multiple parameters that need to be considered. These parameters (human, environmental, ethical, cultural, etc.) generate a new operational complexity, which is yet to find its place among the traditional considerations related to commercial transactions. As a result, it is much easier at the moment to ensure that the right quantity of products will be delivered at the right time or that technical, logistical or financial conditions stipulated in the contract are respected.

Assessment Benchmarks

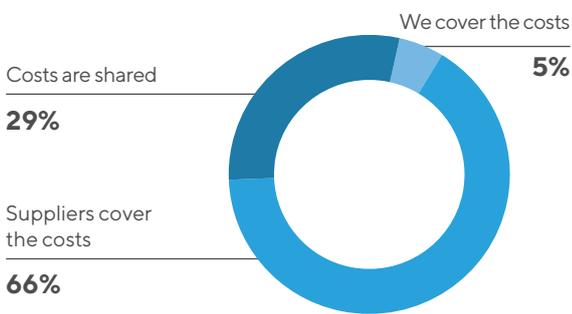
BUYERS

How do you check compliance with the CSR clause?

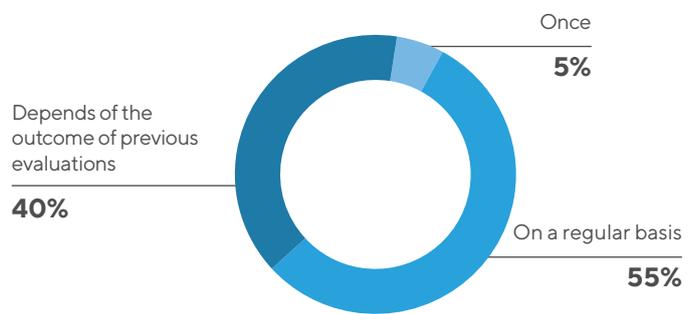




Buyers: managing assessment costs



Buyers: assessment frequency



Supplier Survey Fatigue Becoming a Material Cost

The study found that a growing number of requests for CSR assessments, which suppliers are faced with, is one of the key reasons why they may be reluctant to sign a contract including a CSR clause. Answering questionnaires and dealing with auditors simply requires more resources than they are able to allocate.

“ We are finding that an increasing number of clients have CSR requirements in their contracts, however, very few want to account for these requirements in pricing discussions. This is not an issue where their contractual clauses align with global standards, however, it may create some challenges where the clients have their own unique set of standards to be followed.

There is far too much duplication on requests for corporate responsibility. A company should have their own information pack and that should be issued to customers, not having to fill our endless numbers of different questionnaires.

Comments from the supplier survey

Recommendations: Ensuring Efficient Follow-Up

If a CSR clause stipulates a requirement for an audit or assessment, this need has to be clearly indicated in the contract. The fact that a supplier agreed to follow CSR standards does not mean in itself that they are obliged to be evaluated about it.

“ Clients have to be cautious while drawing the perimeter assessed by third party auditors

Peter Herbel, Partner at Herbel Avocats, former Legal Director, Total Group

Prioritize

Some form of suppliers' CSR performance monitoring is essential when including a CSR clause in the contract, however, for companies with as many as several thousands of suppliers the task would be immense, if not unrealistic. This is when supplier risk mapping proves particularly useful as it allows buyers to identify those who are high risk and adapt the level of monitoring accordingly. Once again, then, prioritization is crucial to effectively implement a CSR clause.

“ We do not expect immediate perfection from companies, We want to be convinced of the consistency and relevance of their due diligence mechanism.

Phillippe Léveque, Executive Director of CARE, France

Share Assessment Costs

A fair distribution of CSR compliance costs is likely to determine the effectiveness of a CSR clause. It is recommended not to burden the supplier with all the costs related to a CSR assessment. This kind of practice may result in a contractual imbalance and lead to the supplier withdrawing from the agreement. In addition, if a buyer agrees to cover at least some of the costs associated with a CSR assessment it shows they take the clause seriously and this works as an additional encouragement for suppliers to comply with it.

Share Assessments

Suppliers are reluctant to undergo multiple CSR assessments, especially that these assessments may sometimes differ or even contradict one another. At times, this extra burden may lead to suppliers withdrawing from commitments or choosing not to commit, even though they do see the need for CSR compliance. The key to solving this problem lies in shared assessments. In fact, there are multiple advantages to shared assessments: they allow for a distribution of costs between buyers and foster greater efficiency among suppliers in their compliance procedures.

“ Shared assessments organizations constitute a solution to improve operational efficiency as well as optimize the costs.”

Maylis Souque, General Secretary at the French National Point of Contact of the OECD

Focus

Negotiating with a direct supplier a possibility to assess or audit their suppliers may be a

delicate matter. This is when covering the cost of assessments may be critical to securing consent. And shared assessments -- both, in terms of costs and results -- make it easier to access suppliers further down the value chain.

Assessments and audits are more likely to be successful if they are not announced and the reports are shared promptly with all the partners.

“ An agreement between large buying companies should not be regarded as a subject of competition. Because it is the interest -- well understood -- of global companies to develop good contractual practices.

Jean-Claude Javillier, former Director of International Labour Department, ILO

“ Smart contracts, supported by the blockchain technology, make it possible to automate certain key due diligence tasks; reporting alerting, reminders, automatic sanctions, etc.

Mustapha Mekki, University of Paris 13, Sorbonne-Cité

Future Considerations

	BASIC	PROGRESSING	ADVANCED	FUTURE CONSIDERATIONS
Enforceability	None or supplier self assessment	Assessments provided by third parties	Assessments provided by third parties regularly	Shared multi-stakeholder assessment instruments BlockChain Tech

- ✓ **Establish KPIs of due diligence shared with stakeholders**
to optimize the effect of the CSR clauses at the level of a territory, a category of purchase or a precise theme.
- ✓ **Share the effort of control**
to reduce costs and involve suppliers.
- ✓ **Involve local stakeholders**
to get a more accurate image of the reality on the ground and build adapted answers.
- ✓ **Use new blockchain technologies**
to get reliable ESG product tracking for consumers and guarantee personal data protection.

Apart from organizing the essential phases of assessments, the efficiency of the CSR clause rests also on the quality of the relation between buyer and supplier. Favoring a cooperative approach over a punitive approach becomes a factor of legal certainty and operational efficiency that the clause must organize.





Cooperation Between Buyers and Suppliers as Key to Effective Implementation

To ensure that a CSR clause is efficient, it is essential to include mechanisms of cooperation that will prevent breach from the supplier and avoid having to terminate the contract.

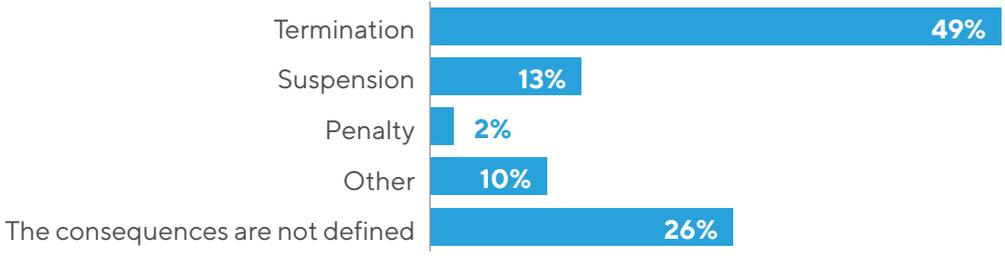
Survey Results: Penalties and Cooperation

Penalties Are Rarely Used

The study found that 75 percent of CSR clauses define the consequences of their breach. This includes 45 percent listing termination as a possible consequence, 10 percent suspension of the contract, with the remaining respondents quoting various other penalties.

BUYERS

What are the consequences in the event of breach of the CSR clause?



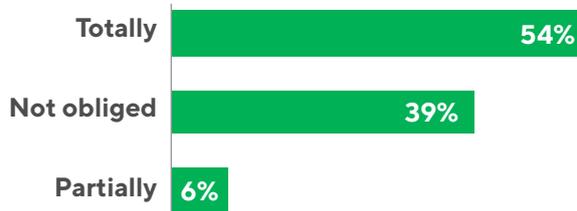
At the same time, however, these penalties are rarely used, with only 16.5 percent of companies saying they have had to resort to them. As many as 30 percent of organizations state that the main challenge regarding a CSR clause is that it is too costly to alter the contract, even if the commitments are not respected.

However, including possible penalties in the contract contributes to the perception that the CSR clause is binding and enforceable. This is particularly important given the fact that suppliers do not always assign the same weight to CSR clauses as they do to the other parts of the contract.



SUPPLIERS

How obliged do you feel to respect these clauses?



The survey revealed that only 54.3 percent of suppliers perceive CSR clauses as legally binding. 39.3 percent answered that they felt partially bound, considering the clauses as “loose guidelines”. A small group of the respondents (6 percent) felt the CSR clause is not binding at all and is merely used as a “communication tool.”

Following in-depth interviews with the suppliers who felt the CSR clause was not binding, or only partially binding, the study identified a number of reasons behind this attitude. They include the feeling that buyers impose too much responsibility on them, unrealistic CSR requirements given their limited resources and – as a result of the latter – the perception that this practice constitutes “green washing.”

For others, the feeling to be partially bound comes from the obvious character of the demands. When the contract is only repeating the law, the supplier does not attach importance to it.

 *The buyers just want to put the clause in all their contracts for their green washing process. They do not care about reality, they do not mind our difficulties or the progress that we are making. It does not seem very binding.*

A comment from the supplier survey

 *We need to have equality guidelines and people know their rights, so I feel some of the clauses more self-evident than as a real guideline. Thoughts with partially bound were about not really paying attention to these because I feel things are ok and just read through the clauses. It does not mean that I do not care if there is a problem with these issues.*

A comment from the supplier survey

Buyers and Suppliers Find More Ways to Work Together Than Listed in the Contract

Looking at cooperation between buyers and suppliers the study found that there are two good practices that are used overwhelmingly by the respondents: more than 80 percent of buyers encourage long term relationships with their suppliers and more than 70 percent include corrective action plans following assessments.

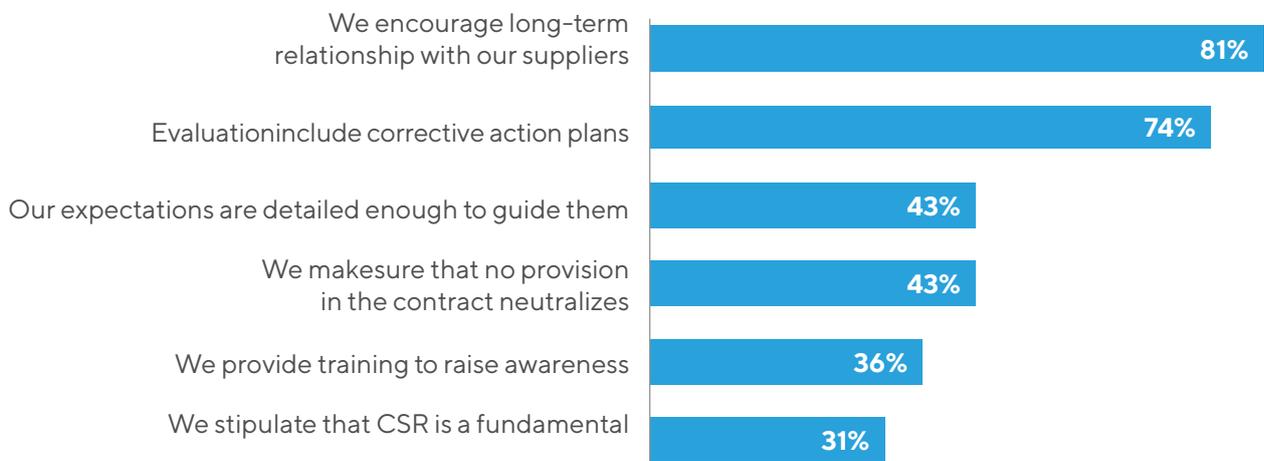
“ Suppliers need long-term contracts to ensure sustainability.

OCDE Debates, Forum on Due Diligence in the Garment and Footwear Industry (January 2018)

Other good practices listed are not nearly as popular. Only one-third ensures that the balance between CSR and other clauses is respected by stating that CSR is a fundamental element of the contract or by verifying that no other contractual provisions contradicts the effect of the CSR clause. Only one-third again provides training to suppliers to raise awareness on CSR issues.

BUYERS

Do you apply the following good practices?



From the suppliers' perspective, the study revealed a good practice on the level of detail, since half of them have already received very specific instructions on the CSR requirements.

SUPPLIERS

Have your customers ever applied the following good practices?



However, these results need to be compared suppliers' responses, which show lack of cooperation from buyers, with almost half of the suppliers facing challenges related to being able to combine CSR compliance and maintain the same level of production.

SUPPLIERS

What are the main challenges faced in the execution of CSR clauses?



SUPPLIERS

Has a buyer ever had high CSR expectations, while requiring a price, quantity and delivery time that could not be accommodated?



“ We are finding that an increasing number of clients have CSR requirements in their contracts, however, very few want to account for these requirements in pricing discussions.

A comment from the supplier survey

Recommendations: Organize Contractual Cooperation to Avoid Breach

Some of the most mature organizations say they favor long-term relationships, which, they believe, guarantee better CSR performance.

Leveraging CSR performance over time requires suitable contractual arrangements, which ensure the best possible conditions for both parties to achieve their objectives.

But other than being enforceable, the operational effectiveness of the CSR clause requires

contractual and societal engineering to organize four fundamental parameters:

- ✓ **Fair allocation of responsibilities;**
- ✓ **Incentivizing contractual conditions;**
- ✓ **Non-judicial grievance mechanism;**
- ✓ **Progressive consequences of clause breaches.**

Fair Allocation of Responsibilities

Organizing contractual cooperation requires looking at how the contracting parties share responsibility for CSR performance. To achieve this, contracts must avoid clauses that may introduce contractual imbalance, including:

- The ones labelled “the supplier commits to (...)”, without any reciprocal obligation from the buyer;
- The ones making the supplier exclusively responsible in case of reputational harm or damages to third parties;
- The ones authorizing unilateral termination without notice.

Obligations must be carried by both parties, in order to avoid a significant imbalance resulting from the CSR clause.

Incentivizing Contractual Conditions

Effective cooperation between buyers and suppliers is crucial throughout their contractual relationship. It is therefore essential for buyers to ensure the right conditions for suppliers to meet their CSR requirements. These conditions can be met through ensuring several commercial parameters: the duration of the contract, the purchase price, the frequency or the volume of order.

To help improve CSR performance, it is possible to consider financial and commercial incentives related to supplier performance. It may even be advisable to help the supplier to mobilize the necessary resources to bring it into compliance. The provision of expertise, the identification of relevant field stakeholders, cash facilities, and even the direct contribution to financing compliance costs can be considered.

 *Customers mostly negotiate a contract and then add the CSR requirements later - so they are not costed in the contracted price.*



A comment from the supplier survey

 *The Bangladesh Agreement requires from brands to ensure that their suppliers have the financial capacity to respect the norms of the Agreement and to maintain a long-term relationship with them.*

Joris Oldzendiel, Deputy Director of Implementation, Bangladesh Accord Foundation

For suppliers meanwhile, this cooperation may be characterized by ensuring greater transparency and visibility into their own suppliers, apart from basic contributions such as ensuring access to their production sites.

Certain sensitive clauses are identified as potentially interfering with the CSR clause, among them the conformity clause, the delivery conditions (Incoterm Delivery Duty Paid) or even the coverage of the supplier's insurance.

Note

The success of this logic of contractual cooperation also raises the more general question of the coexistence of a CSR clause with the other contractual requirements. It must be ensured that no other contractual provision contradicts the expected effects of the CSR clause.

It should be noted that legally, if the CSR clause conflicts with another obligation, it is the one that will most often be contradicted because it is not considered as an essential element of the sales or supply contract.

Amicable Dispute Resolution

A clause on amicable dispute resolution is recommended in case difficulties arise during the execution of a CSR clause or with its interpretation. This can take a form of a mediation. Conducted by an independent third party, jointly appointed by the supplier and the client, mediation also contributes to the involvement of a third party in the contract in order to optimize the treatment of the disputed subject. Depending on the nature of the dispute, it may be a stakeholder in the field (NGO, trade union, etc.), a person with specific expertise adapted to the ESG issue raised or an institution such as OECD through its National Contact Points (NCPs).

More generally, it is recommended to indicate that negotiations must be carried in good faith to obtain a fair settlement.

“ *We recommend parties to favour mediation compared to the intervention of a judge in case of difficulty of interpretation or implementation of a CSR clause.*

Françoise Odolant, Head of Purchasing, Charters and Labels Division, MEIN

Progressive Consequences of Clause Breaches

A system of progressive consequences includes, as a first step after a breach, a corrective action plan, followed by a suspension of the contract, then penalties and finally termination.

CSR clause breaches are usually revealed during a supplier assessment. When this happens, a corrective action plan, involving the supplier, must be put in place. This system accompanies the supplier in its compliance process in a collaborative approach and not a punitive one. The cost of compliance and corrective actions resulting can be shared to demonstrate a real effort of cooperation.

““ *Field-based NGOs are relevant stakeholders to involve within the elaboration and implementation of corrective action plans.*

Joseph Wilde-Ramsing, OECD Watch

Then, in case of material breach (for instance refusal of assessment), the suspension of the contract may be called for:

““ *Suspension of contract in case of breach should be encouraged rather than termination.*

OCDE Debates, Forum on Due Diligence in the Garment and Footwear Industry (January 2018)

In addition to termination and suspension, it is also possible to plan that the supplier should pay penalties in case of breach of the CSR clause. The amount of penalties may be gradual, depending on type of the violation.

Finally, as a last resort, buyers may choose to terminate the contract. However, if the contract does not stipulate termination as a possible penalty in case of a CSR clause breach such termination may prove very difficult. It is therefore recommended that the contract include the possibility of termination, even if it is to be used as a last resort.

““ *One of our supplier was not complying with the clause, but in the absence of terms in the contract, we had to negotiate termination. Now, we specify that a material violation can lead to an early termination.*

Marleen Van Mensel, Senior Lawyer at Solvay

Termination must be accompanied by a reasonable prior notice and the possibility for each party to make their argument.

““ *Termination of a contract for breach of the CSR clause can lead to major damages on the local economy if the supplier is forced to fire its employees due to the loss of an important client.*

OCDE Debates, Forum on Due Diligence in the Garment and Footwear Industry (January 2018)

Future Considerations

	BASIC	PROGRESSING	ADVANCED	FUTURE CONSIDERATIONS
Enforceability	Not defined	Possible penalties	Progressive steps to follow in case of breach	Allocation of responsibilities among stakeholders Dedicated insurance policies
Consistency	Isolated CSR clause	Formalized consistency between CSR and business demands	Operational consistency	Sustainability issues as a key element of a business contract Sustainable Contract Principles Sustainable Contract KPIs

- ✓ **Achieve a fair allocation of responsibilities**
to generate a relation buyer/supplier win-win
- ✓ **Optimize integration of the CSR clause with other clauses**
for a legal constraint guaranteeing legal certainty
- ✓ **Elaborate contractual diligence KPIs**
to follow-up the use of contracts in the CSR approach





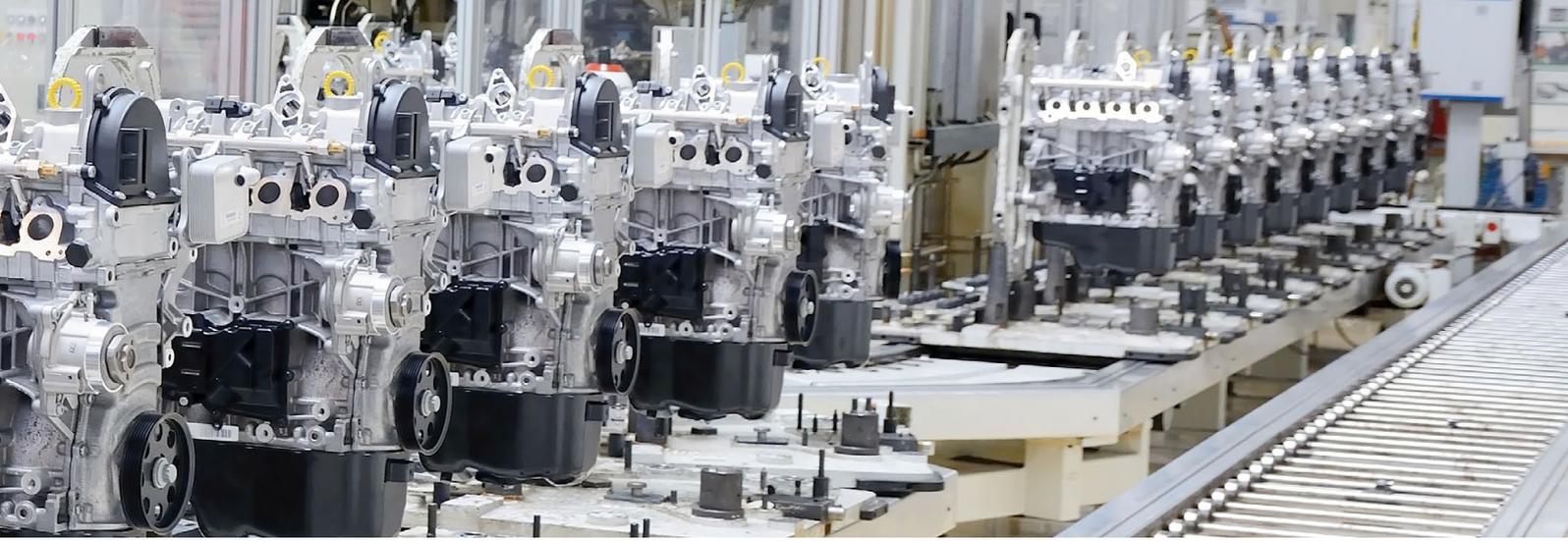
Toward a More Effective Contractualization



The analysis of a wide range of clauses combined with the cross-study Suppliers Buyers enabled us to define six criteria, three levels of performance associated - from Basic to Advanced - and the challenges ahead. While it is possible to understand each of these criteria separately, in reality they are all intrinsically linked to measure the effectiveness and maturity of a CSR clause.

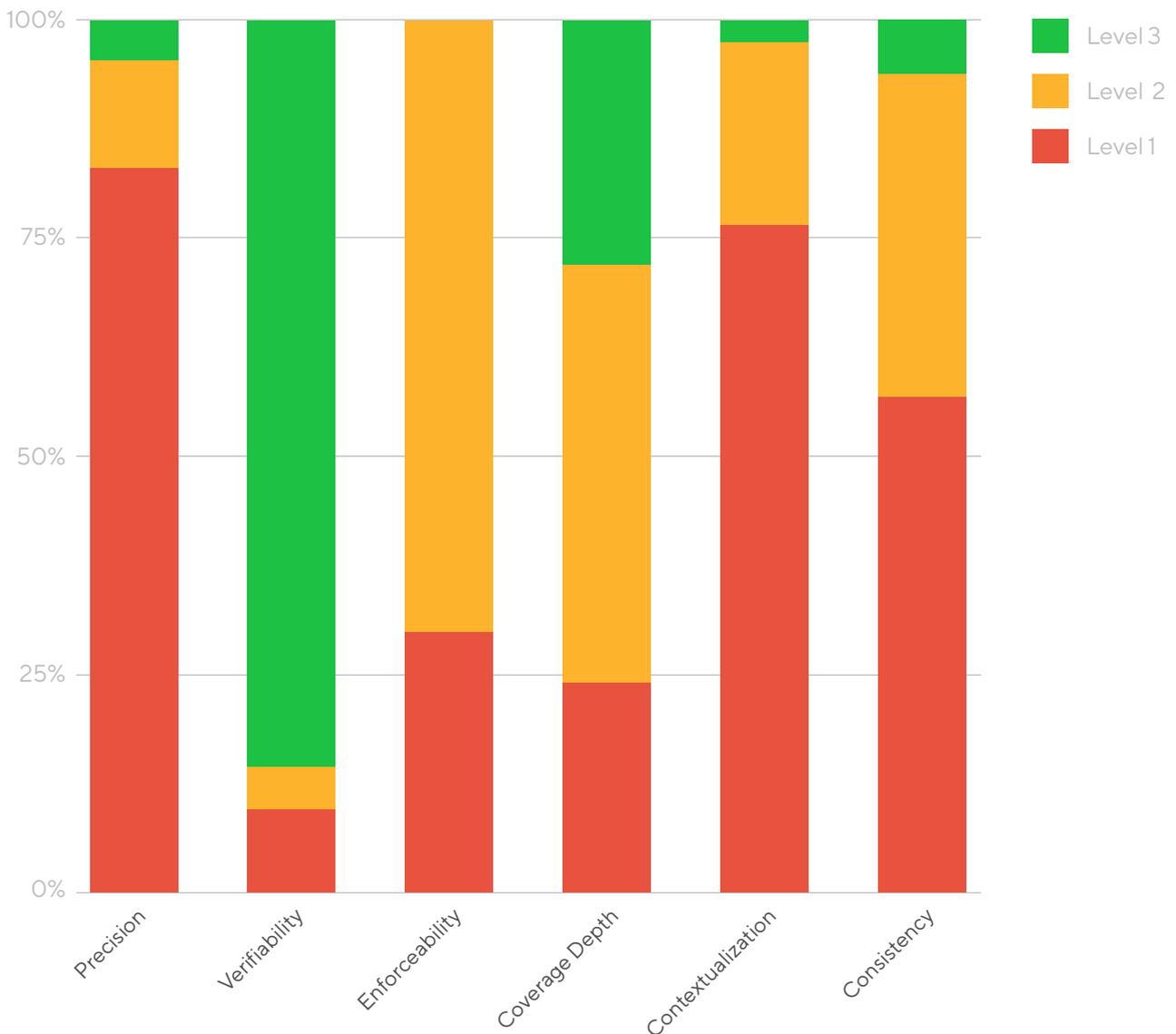
Different levels corresponding to each feature can be summarized as follows:

	BASIC	PROGRESSING	ADVANCED	FUTURE CONSIDERATIONS
Precision	General principles	Policies expected	Objectives settled	Sector- and country-specific ESG issues and dedicated diligence instruments
Verifiability	None or supplier self assessment	Third-party assessments	Third-party assessments conducted regularly	Shared assessment devices BlockChain Tech / Smart Contract
Enforceability	No consequences defined in case of breach	Possible penalties in case of breach	Progressive steps to follow in case of breach	Allocation of responsibilities among stakeholders dedicated insurance policies
Coverage Depth	Partial coverage of tier-1 suppliers	All high-risk tier-1 suppliers	+Beyond tier-1	Full coverage of the "sphere of influence"
Contextualization	None	By size / sector	+Based on risk mapping / analysis	Case-by-case adjustments with individual ESG progressive agenda according to convened prioritization
Consistency	Isolated CSR clause	Formalized consistency between CSR and business demands	Operational consistency	Sustainability issues as a key element of a business contract Sustainable Contract Principles Sustainable Contract KPIs



What Does a Typical CSR Clause Look Like?

Sustainable contract diagnostic: survey results*



*It has to be noted that the level of maturity corresponds to particularly advanced companies in terms of CSR and does not reflect the general level of contracts.

Based on these results we can infer that a **typical CSR clause** has the following characteristics:

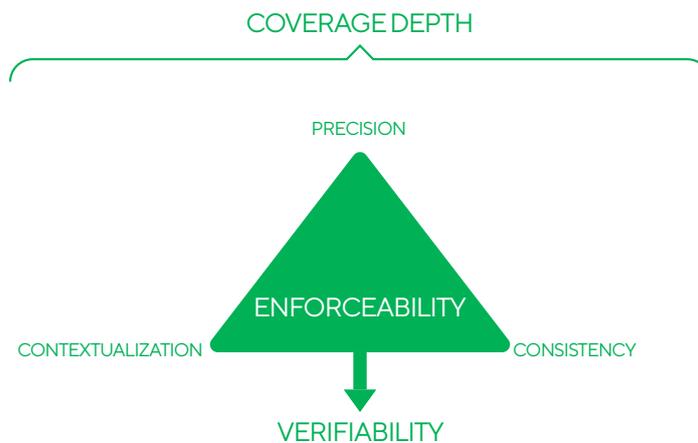
Little precision: A typical clause only refers to general principles. This, however, may be compensated by **verifiability** with regular assessments of how the clause is executed.

The coverage extends to tier-2 suppliers and beyond: Parties are able to visualize all the links of the supply chain that need to be addressed.

It is not enforceable: Even if it lists termination as a possible consequence in the event of breach it is necessary to ensure that such provision is valid and to plan a progressive penalty system to encourage cooperation between the parties.

Resorting to a standard CSR clause jeopardizes its integration with the contract - contextualization and consistency are the key parameters, likely to result in notable progress and innovation in CSR contractualization.

The analysis criteria are intrinsically linked to one another.



Future Considerations

In Search of Effective Contractual Practices Around CSR

- ✓ Contracts will likely become the most effective tool demonstrating CSR diligence.
- ✓ CSR clause enforceability no longer guarantees legal certainty.
- ✓ CSR clauses must be negotiated and understood by suppliers. In addition, adaptation to context is crucial in ensuring cooperation and to effectively address ESG issues.
- ✓ Ensuring compatibility with other requirements stipulated in the contract is essential.
- ✓ Operational effectiveness of a CSR clause is contingent on normative engineering.



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Annex 1: What Next?

Methodology and Survey Participants

The quantitative survey was conducted online among 569 companies between November 16, 2017 and January 12, 2018 followed by 20 in-depth interviews in the same time period.

Two surveys

Two surveys were conducted among two different audiences. This allowed us to capture two perspectives: that of large companies, who typically drive CSR requirements in contracts, and that of suppliers to whom these requirements are addressed. We want to thank them for their participation and their involvement during our interviews.

Buyers survey

The buyer survey was conducted among EcoVadis' most mature customers in order to collect good practices from companies who integrate CSR into their procurement contracts.

50 of them completed a detailed questionnaire on their CSR clauses. Most of these companies are located in Europe and some are based in North America and Australia. They are large companies, 60 percent of them having an income in excess of 5 billions of dollars.

Suppliers survey

As is the case with all surveys, the results of this study were likely influenced by self-selection bias (buyers with well-developed CSR clauses and best performing suppliers being more likely to participate). This minimal level of bias has always been expected and observed in our studies.

The Sustainable Contract Diagnostic Tool

The Sustainable Procurement Diagnostic Tool (Part II) is designed to give a broad orientation on the maturity of various contract components, from "basic" to "advanced" levels, and is by no means an exhaustive or universally applicable model.

As is common in survey research, the 2017 Barometer Survey results were likely influenced by self-selection bias, resulting particularly from mature and benchmark-level SP professionals (i.e., SP professionals in mature programs feeling 'extra' motivated to participate). This minimal level of bias has always been expected and observed in the Barometer research survey series.

Annex 2:

Toward Shared Sustainable Contracting Principles

In addition to revealing shortcomings and challenges surrounding contractual practices related to CSR, the study has also provided an opportunity to devise innovative solutions such as *Sustainable Contract Principles* developed by Affectio Mutandi.

What Is a Sustainable Contract?

A sustainable contract is any contract which in its objectives and execution, includes the economical, social and environmental aspects in to protect fundamental rights and the environment.

“ *Contract law could establish a right for a sustainable contract.*

—
Muriel Fabre Magnan, University of Paris 1 Panthéon-Sorbonne

“ *Including CSR-related clauses in procurement contracts may result in a risky paradox: the buyer expects the supplier to take full responsibility and to offer a low price. In this ambiguous context, characterized by relationships that are often unbalanced, the Sustainable Contracting Principles help commercial partners to build fair relationships based on the idea of shared responsibility and shared risk.*

—
Olivier De Schutter, University of Leuven and member of the UN Committee on Economic, Social and Cultural Rights

“ *These Sustainable Contracting Principle could allow companies to better accomplish their CSR demands, for instance in public-private partnerships in Africa, which is an important topic for us.*

—
Stéphan Alamowitch, Senior Partner and Director of Financial Department, UGCC Avocats

The effective consideration of CSR issues into commercial relationships has become an inescapable challenge since the new social and legal expectations. They are catching the attention of multiple stakeholders, from institutions to NGOs, to investors.

In this context, companies must demonstrate a contractual diligence, proving that they identify the ESG risks linked to a commercial transaction, that they are able to react to it and report on it.

So far, if the use of CSR clause has spread, organizations are not provided with a common base of principles to refer to. The time has come to establish shared principles that, like the Principles for Responsible Investment (PRI), will allow generalization of practices guaranteeing an efficient contractualization of CSR stakes.

It is the objective of the Sustainable Contract Principles that draw lessons from the current practices and are intended to apply regardless the origin of the buyers and the suppliers.

These principles are intended to engage parties to the contract but also any other relevant stakeholder likely to play a part in the prevention, mitigation and reparation of ESG impacts: unions, NGOs, rating agencies, associations.

Sustainable Contract Principles are a way for contracting parties and any stakeholder to exert a positive influence on the CSR practices linked to a business contract.

By signing the *Sustainable Contract Principles*, contracting parties and stakeholders pursue the objective to identify, prevent, repair and report on any negative incidence on environmental, social or governance aspects occurring on the supply chain.

To do so, contracting parties and stakeholders commit to respect OECD guiding principles for multinationals, UN guiding principles and the human rights convention they are based on, the ILO Declaration and fundamental conventions, and the ISO 26000.

By adhering to the *Sustainable Contract Principles*, contracting parties and stakeholders:

Declare employing all reasonable means to:

- Identify all material CSR risk, including in the supply chain, resulting from the contract;
- Implement whistle-blowing mechanisms and control mechanisms adapted to the risks identified;
- Organize the effective interaction of all stakeholders;
- Adapt the contractual relation in case of major ESG incidence.

Commit not to:

- Exclude all forms of personal liability in the even of ESG damage;
- Burdening one contracting party with the entire financial cost of due diligence measures;
- Undermine directly or indirectly the capacity of the contracting party to fulfill the ESG requirements;
- Terminate the contract unilaterally, without notice, in case of breach of CSR commitments.

Commit to:

- Always act in good faith and in a spirit of collaboration;
- Allocate reasonably responsibilities for ESG risks;
- Contribute to finance diligence tools that are reasonable and effective;
- Share diligence tools with stakeholders;
- Report to stakeholders on ESG performance as per the contract.



About EcoVadis

EcoVadis is the first collaborative platform providing sustainability ratings and performance improvement tools for global supply chains. EcoVadis' easy-to-use CSR scorecards help companies to monitor suppliers' environmental, ethical, and social practices across 150 purchasing categories and 110 countries. Over 150 industry leaders such as Nestlé, GSK, Heineken, Michelin, Johnson & Johnson, Schneider Electric, L'Oréal, BASF, and Subway, and over 30,000 of their trading partners use EcoVadis to reduce risk and drive sustainability and innovation.

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About Affectio Mutandi

Affectio Mutandi is the first agency specializing in strategy on environmental, social and governance (ESG) issues. It offers an innovative, hybrid approach to CSR, crisis and corporate communication, public affairs, legal counseling and NGO relations, essential for organizations facing the challenges of a globalized world and an evolving normative landscape.

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