SPECIAL ESSAY

Shifting Modes of Labor Regulation in Global Supply Chains

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EXECUTIVE SUMMARY

This essay outlines the changing modes of regulation of labor conditions in global apparel supply chains, which are mostly concentrated in Asia; assesses the effectiveness of 25 years of private voluntary regulation by global firms; and examines critically the implications of new European regulation now mandating what was previously a voluntary corporate activity.

MAIN ARGUMENT

Asia is the global center of apparel production, with Bangladesh, Cambodia, China, India, Indonesia, Pakistan, and Vietnam all being major exporters. Since the 1990s, activist pressure in developed country markets has forced global apparel and footwear companies to adopt voluntary methods to ensure that their products are not made under sweatshop conditions. Companies developed codes of conduct for the first-tier factories in their supply chains and found ways to audit whether supplier factories were in compliance. However, this voluntary private-regulation model has not been adequate to alleviate labor and workplace concerns in global apparel supply chains. A shift from private regulation to public regulation—the beginning of which may be currently underway in the European Union with the recent introduction of mandatory due diligence legislation—may prove to be a more effective means of bettering labor rights and conditions.

POLICY IMPLICATIONS

• If the recent EU legislation allows global companies to be legally liable for violations of mandatory due diligence requirements regarding labor rights and conditions in supply chains, a sea change in worker rights and labor practices could occur.

• The new legislation would require global companies to adopt more responsible purchasing practices so that their practices are not responsible for labor violations.

• The EU legislation could have an impact on sourcing locations, as companies compete for locations that are more likely to provide institutional environments with lower risk of violations. Global suppliers would have a greater incentive to take the high road in terms of employment practices to obtain more business from European buyers. National governments in apparel-exporting countries may be motivated to improve enforcement of labor regulations.
The world’s clothes are made in Asia. The supply chains of the global garment and apparel industry are mainly concentrated in South and East Asian countries, including Bangladesh, Cambodia, China, India, Indonesia, Pakistan, and Vietnam. Naming and shaming campaigns by NGOs tying Nike and other companies to sweatshops and the use of child labor in the early 1990s provided the impetus for the development of private-regulatory efforts by global athletic shoe and apparel retailers. Activist pressure in developed country markets forced these companies to adopt voluntary methods to ensure that their products are not made under sweatshop conditions. However, it was both governments and NGOs that helped organize companies to join multi-stakeholder institutions in private regulation. For example, the Clinton administration provided leadership and funding to start the Apparel Industry Partnership, which later became the Fair Labor Association; NGOs such as Social Accountability International, the International Labor Rights Fund, and U.S. labor unions were also involved in that effort.

This essay draws on findings from my book *Private Regulation of Labor Standards in Global Supply Chains: Problems, Progress, and Prospects*, which provides data obtained from forty thousand audits of companies in global apparel supply chains conducted over seven years in more than twelve countries and thirteen industries, as well as data from several global companies. The book represents the first comprehensive and generalizable evidence about whether private regulation has actually improved the lives of workers in global supply chains. The results show (1) no improvement in the number of code of conduct violations over time for multiple labor issues, (2) that actual wages in the supply chains are far from the levels promised by global brands, (3) retailers and multi-stakeholder institutions are inconsistent in the application of their codes, and (4) that the core labor right of freedom of association and collective bargaining—an enabling right that affects all other worker rights—is rarely if ever adhered to or that companies are sourcing from countries where the institutional conditions for this right are not favorable (for example, China). In sum, private regulation has not proved to be very effective in furthering workers’ rights and conditions in the global apparel industry. The remainder of the essay is organized as follows:

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The most common form of the private-regulation model has three elements: setting standards regarding labor practices in global supply chains through a corporate code of conduct that is generally based on the core labor rights conventions of the International Labour Organization (ILO), auditing or social auditing that involves monitoring whether supplier factories comply with the code of conduct, and incentivizing suppliers to improve compliance by linking future sourcing decisions to their compliance records (i.e., penalizing or dropping noncompliant suppliers and rewarding compliant ones).

Since the early efforts in the 1990s, we have seen explosive growth in the adoption of private regulation. From beginnings in apparel and footwear (for example, among Nike, Gap Inc., and Adidas), efforts at private regulation have diffused to many other industries over the past two decades—horticulture, home furnishings, furniture, fish, lumber, fair trade coffee, and others. One study found that more than 40% of publicly listed companies in food, textiles, and wood products had adopted the private-regulation model.

This diffusion has created a large and growing ecosystem of actors and institutions. Multi-stakeholder initiatives have led to a “collective fora” for private regulation. A growing number of auditing organizations—Verite, Intertek, and ELEVATE, for example—conduct social auditing for global supply chains.
companies and multi-stakeholder initiatives, claiming their services help improve private regulation and labor conditions in global supply chains. Social auditing is an $80 billion industry, and “hundreds of thousands of audits are conducted on behalf of individual firms and multi-stakeholder initiatives each year.”⁶ There are well over two hundred auditing programs, not including those run by the brands themselves. A rough estimate suggests that the top ten auditing firms account for more than 10% of this total.⁷

The growing private-regulation industry has become the focus of a wide range of actors. It has given birth to critical NGOs that use investigative reporting to pressure brands to improve their performance on labor standards (e.g., Oxfam and Labour Behind the Label). Other organizations facilitate the exchange of audit information among global companies (e.g., Sedex) and provide myriad consulting services to global brands and supplier factories. There has also been a rise in international organizations and institutions seeking to foster improvements in labor conditions in global supply chains, such as the ILO’s Better Work program (a collaboration between the ILO and the International Finance Corporation), the UN Global Compact, and a variety of business and human rights organizations. Socially responsible investment companies actively engage in evaluating private-regulation programs. And a steadily increasing number of organizations, such as the Sustainable Apparel Coalition and the Better Buying Initiative, work to improve the efficacy of private regulation by layering new policies onto the basic model. At the same time, university centers have emerged that are devoted to private regulation and workers’ rights, and the number of scholarly books, special issues of journals, and articles devoted to the subject continues to grow.

Of course, private regulation would not have been necessary had garment-exporting countries enforced their labor laws. Most, if not all, exporting countries are members of the ILO and have adopted labor laws consistent with its conventions. Yet the ability and willingness of apparel-exporting countries to enforce their laws has been a key problem. Some governments view low labor costs and standards as a source of competitive advantage and a key means of attracting the apparel industry. In some cases, this economic argument is correlated with the suppression of labor rights and standards for political control, while in others, the state has been captured by elites who are also owners of apparel factories. Many apparel-exporting countries are poor and do not possess the administrative

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⁶ Short, Toffel, and Hugill, “Beyond Symbolic Responses to Private Politics,” 2.
⁷ Kuruvilla, Private Regulation of Labor Standards in Global Supply Chains.
and financial capacity to provide effective law enforcement and to sustain a
good labor inspection regime with well-trained labor inspectors. To fill the
regulatory void in exporting countries, brands have sought legitimacy with
their critics in developed country markets through private-regulation policies.

HAS PRIVATE REGULATION BEEN EFFECTIVE?

Has private regulation brought about meaningful improvements in
working conditions in the global supply chain over the last 25 years? The
answer to this question must be gleaned from case studies, actual events, and,
more recently, quantitative research.8

Summing up the case-study research over the last fifteen years, one group
of researchers noted the following:

Existing evidence suggests that they [codes of conduct] have had
some meaningful but narrow effects on working conditions and
the management of human resources, but the rights of workers
have been less affected, and even on the issues where codes tend
to be most meaningful, standards in many parts of the [apparel]
industry remain criminally low in an absolute sense.9

Other summaries suggest that the improvements are unstable and limited in
the case of working conditions such as health and safety, and that there have
been no improvements in freedom of association and collective bargaining
rights.10 Additionally, there has been a general absence of steady progress
in compliance over the years, with apparel supplier factories cycling in and
out of compliance. Even Nike, a leading firm that pioneered the adoption of
the private-regulation model, has shown no clear evidence of improvement
over time.11 Factory disasters in Bangladesh and Pakistan have been a
testament to the ineffectiveness of private-regulation efforts. Most of the
disasters in apparel factories—for example, at Rana Plaza in Bangladesh,
where the collapse of an eight-story building killed more than 1,100 workers

8 As mentioned in the introduction, my book examines data obtained from companies and audits
of companies in global apparel supply chains in a variety of countries in greater detail than can be
presented here. See Kuruvilla, Private Regulation of Labor Standards in Global Supply Chains.
9 Tim Bartley et al., Looking behind the Label: Global Industries and the Conscientious Consumer
10 See, for example, Richard M. Locke, The Promise and Limits of Private Power: Promoting Labor
Standards in a Global Economy (Cambridge: Cambridge University Press, 2013); Judith Christina
Stroehle, “The Enforcement of Diverse Labour Standards through Private Governance: An
Assessment,” Transfer: European Review of Labour and Research 23, no. 4 (2017): 475–93; and Mark
Anner, “Corporate Social Responsibility and Freedom of Association Rights: The Precarious Quest
11 Locke, The Promise and Limits of Private Power.
in 2013—had been repeatedly inspected under the social auditing programs of the brands and retailers.

Explaining the Failure of Private Regulation

What explains the lack of sustainable progress in improving working conditions? The answers can be found both in conceptual problems with the design of the private-regulation model and in its real-world implementation by global corporations. In terms of design issues, there is often an assumption that global buyers have the leverage to force suppliers to comply with their codes of conduct or otherwise change their practices to improve labor conditions. In apparel, it is common for factories to each produce for several brands, which allows them to spread risk and insure themselves against an unforeseen change in consumer demand for any single brand’s product. This reduces each brand’s leverage over factories. Another faulty assumption is that the interests of the different actors in the supply chain are aligned through a system of incentives. Typically, relationships between buyers and suppliers are antagonistic rather than collaborative, and buyers and suppliers often have conflicting interests. Buyers want suppliers to invest in improving labor standards but consistently squeeze suppliers with lower prices for their product, thus prompting suppliers to hide or falsify compliance data.

As for implementation, empirical investigations have identified problems with each of the three components of the private-regulation model: codes of conduct, auditing, and incentivizing compliant behavior among suppliers. Regarding the first component, codes of conduct, there is a multiplicity of codes across companies and multi-stakeholder initiatives that may focus on the same standards but differ as to the thresholds of acceptable behavior. For example, companies belonging to Worldwide Responsible Accredited Production (WRAP), a multi-stakeholder organization dominated by companies, are required to ensure that at least minimum wage is paid to supply chain workers, whereas company members of the Fair Labor Association (another multi-stakeholder association) are required to ensure that wages paid are sufficient to cover basic needs and some disposable income for workers. This disparity between codes results in a multiplicity of auditing protocols that make it difficult for factories supplying multiple companies to meet differing standards.

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12 Locke, The Promise and Limits of Private Power.
The second component, social auditing, has received the most criticism. Audits are too short to uncover violations—the typical audit is less than two days in a large factory—and auditing is a commoditized, low-paid, outsourced activity. Therefore, auditors, who are typically not well trained in all aspects, need to adequately evaluate the factory (e.g., in both labor rights and chemicals handling) but satisfice by “checking the box” without ascertaining the root causes of violations.

Although interviews with workers are a required component of the auditing process, most involve workers who have been coached to provide desirable answers. There is also considerable fraud and bribery in the process, with auditors “willing to turn a blind eye when necessary to please factory managers.” As I show in greater detail in my book, information provided to auditors is often falsified. In some countries, such as China and India, and some industries, such as apparel, toys, and furniture, audit falsification is rampant. Consulting companies in China, for instance, help factories pass audits through falsification of data and other methods. On the other hand, there is also “audit fatigue,” in which factories servicing multiple brands are tasked with carrying out far too many audits per year and meeting too many variations in standards. Because brands use different auditing protocols and rating scales, it may be possible for a factory to pass one brand’s audit while simultaneously failing a second brand’s audit.

The numerous problems with social audits partially explain the failure of private regulation. In recent years, global brands have promoted a new initiative to reduce audit fatigue for suppliers. Driven by global companies and some suppliers, an organization called Social and Labor Convergence was created in 2015 that committed signatory brands and suppliers to conducting a “self-audit” that is then verified by the organization’s contractors. Although many brands have signed on to this popular framework, this is a retrograde initiative. The verifiers are the same auditing companies that have been criticized in the past, and the model is one in which the suppliers now pay the verifiers, thus failing to improve quality or ensure accountability and independence in the process.

There is also failure in the third component of private regulation—incentivization and the linkage between sourcing and compliance. The thinking was that global buyers would reward factories that showed steady improvement in compliance with more orders and perhaps longer-term

13 Bartley et al., Looking behind the Label.
14 See Kuruvilla, Private Regulation of Labor Standards in Global Supply Chains, chap. 1.
relationships, while factories that did not remediate compliance violations adequately would be “punished” by receiving fewer orders. But relatively little is known about whether companies are in fact incentivizing suppliers to improve compliance because companies have not reported on their efforts to integrate sourcing and compliance and do not share such data. A limited number of studies suggest no integration at all, while one case of such integration took a global retailer almost six years.

Are Global Buyers the Problem?

Only now, after 25 years of private regulation, has attention turned to the big question of whether the violations in supplier factories are not the fault of the suppliers but due to the purchasing practices of global companies. The argument is that sourcing practices are often the root cause of noncompliance. A steady squeezing of the prices paid to suppliers induces them to find noncompliant ways to cut labor costs, and late or short-turnaround orders force suppliers to increase overtime beyond acceptable limits. An ILO global survey of 1,454 suppliers reveals how the purchasing practices of global buyers affect factory working conditions: low purchasing prices, insufficient lead times, and inaccurate technical specifications lead to lower wages and longer hours. In recent years, global attention has focused more on the likely impacts of poor purchasing practices. NGOs have come together to create the Common Framework for Responsible Purchasing Practices that calls on global brands to focus on issues such as lead times, payment terms, more durable buyer-supplier relationships, and so forth—an extensive laundry list of practices that cannot necessarily be easily measured. The focus on purchasing practices has also resulted in initiatives such as Better Buying and the Better Buying Institute, an organization that allows suppliers to “rate” their customers’ purchasing practices along several dimensions, which are then fed back anonymously to global buyers in hopes of improving them. But data that conclusively proves that poor practices and low prices cause

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15 Bartley et al., *Looking behind the Label.*
code of conduct and labor violations is scarce because brands are not required to share information about their purchasing practices and suppliers are not required to share data regarding the orders they receive, their payroll, or their working conditions.

In sum, not only are there faulty assumptions underlying the design of the private-regulation model, but there are a host of implementation issues that are responsible for the model’s failure, despite global companies having practiced it for almost 25 years. One way to think about this failure at a more abstract level is to consider it a decoupling problem. In other words, global buyers could practice two types of decoupling. The first is “policy-practice” decoupling, in which global buyers adopt codes of conduct but are not interested in implementing these codes in any serious way. Although they go through the motions of auditing, they do not focus on remediation and do not connect their sourcing practices to factories’ code violations. This likely explains the host of implementation failures noted above. The second is “practice-outcome” decoupling, in which global buyers are serious about implementing their codes of conduct, but their practices do not result in better outcomes at factories. However, we do not know where or when practice-outcome decoupling occurs, and whether there are in fact successes, because buyers do not report the results of their private-regulation practices in the corporate responsibility reports on their websites. Thus, there is opacity—we do not see what is going on, what works, what does not work, and why it does not work—and that impinges on the ability to identify best practices. Institutional theory suggests that if best practices were visible, more companies would follow them, but the apparel industry so far lacks widespread evidence to support this assumption. I suggest that opacity in private regulation is driven by three factors: behavioral invisibility (the inability to see how suppliers behave due to various auditing problems), practice multiplicity (the variety of auditing and rating scales that obscure supplier performance), and causal complexity (the inability to see cause and effect because companies are not transparent about the impact of their private-regulations programs in different countries).

 Nonetheless, there are some examples of successful private regulation. I document the case of a global retailer where compliance among its suppliers has increased substantially over time. The reason for such an increase was that the global retailer guaranteed orders to these suppliers for six years while giving them time to increase their compliance. As well, I studied the

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19 Kuruvilla, Private Regulation of Labor Standards in Global Supply Chains, 12–14.
20 Ibid., 108–10.
successful integration between purchasing practices and compliance in a global company. Some factories that participate in the ILO’s Better Work Program have improved compliance dramatically over time as program advisers counsel factories about the root cause of their problems. The same data also shows that compliance is much higher in factories with unions and collective bargaining agreements. Another example is evidence provided by Richard Locke regarding Nike factories, where the adoption of lean production not only increased wages but also increased compliance with the code of conduct. There are many other examples of successes in case studies and anecdotes, but they are not widely diffused and known. Increased transparency on the part of the global apparel companies—through either voluntary disclosure about the effects of their programs or legal requirements for disclosure and reporting—will go a long way toward making best practices visible and help to solve the practice-outcome decoupling problem.

FROM VOLUNTARY TO MANDATORY REGULATION APPROACHES

Since 2012, there have been new pieces of legislation in several countries that require companies to address labor issues in their supply chains. These laws fall into two categories—limited and comprehensive. The limited category includes modern slavery legislation in California, the United Kingdom, Australia, and more recently in Canada. The legislation in the first three places only focuses on forced labor in supply chains, while the Canadian legislation focuses on child labor as well. This type of legislation is limited because it focuses only on one or two human rights issues and does not hold companies accountable for violations. The comprehensive category focuses on labor and environmental practices in supply chains. Laws in this category encompass all labor standards and make a stronger effort to hold companies accountable for violations in the supply chain. The first of these laws was enacted in France in 2017, and the second was enacted in Germany in 2021 and implemented in 2023. A third was passed by the European Parliament in 2022, but the different European Union institutions (the parliament, the Council of Ministers, and the EU Commission) have not yet reconciled their slightly different versions of this legislation. In addition, in January

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22 Ibid.
23 Locke, The Promise and Limits of Private Power.
2023 the EU implemented the Corporate Sustainability Reporting Directive, which modernizes and strengthens the rules concerning the social and environmental information that companies must report. While the limited category has not affected corporate respect for labor rights in supply chains to any appreciable extent, the legislation in the comprehensive category could have far-reaching implications, changing the playing field of international labor regulation significantly.

**Limited Legislation**

The California Transparency in Supply Chains Act came into effect in January 2012 and requires companies to publicly disclose their efforts to eradicate human trafficking and modern slavery in their operations. The law applies to retailers and manufacturers doing business in California with worldwide annual gross receipts in excess of $100 million. Companies must disclose their efforts in five areas: (1) the verification of product supply chains to evaluate and address risks of human trafficking and slavery, (2) the conduct of supplier audits to evaluate supplier compliance with company standards for trafficking and slavery, (3) the requirement of direct suppliers to certify that materials incorporated into the products comply with laws regarding slavery and human trafficking of the country or countries in which they are doing business, (4) maintenance of internal accountability standards and procedures for employees or contractors failing to meet company standards, and (5) training on human trafficking and slavery for company employees and management who have direct responsibility for supply chain management. The law also requires that disclosures must be accessible through a conspicuous and easily understood website link.

The California Franchise Board is supposed to send the California attorney general’s office a list of all companies covered by the law at the end of every year. The attorney general’s office then reviews all websites and determines compliance with the act. However, there is no direct penalty for companies that do not follow the law, which only provides for injunctive relief in the case of complaints. Thus, the law does not have teeth but relies on market incentives such as reputation and consumer awareness to influence corporate behavior.

Early evaluations of the law did not provide any positive information as to its efficacy. Know the Chain, an NGO, was only able to identify 19% of the

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companies required to comply with the new law, and of those, only 31% had disclosure statements that covered all five areas. In 2015 the state ramped up its efforts at compliance. A study by Development International concluded in 2016 that the average disclosure compliance score was 60%, and that the extent to which a company reported positive action (an affirmative conduct score) was 30%. Of the companies that reported, only 41% had a disclosure score over 70%. I have been unable to locate subsequent studies or obtain any data regarding the attorney general’s actions connected with this law.

The modern slavery legislations in the UK (the Modern Slavery Act 2015) and Australia (Modern Slavery Act 2018) are modeled on the California act. The UK act requires companies with an annual revenue of more than 36 million pounds to submit a modern slavery statement. While comprehensive data is not available, evaluations by Chartered Institute of Procurement and Supply found that in 2022 only 29% of the organizations required to produce a modern slavery statement submitted it to the government registry, a sharp drop from 46% the previous year. The UK is expected to introduce a bill in parliament mandating compliance, but at the time of writing in late 2023 this bill had not yet been introduced. Likewise, a three-year review of the Australian act conducted in 2022 revealed that the act needed to be “beefed up” and suggests that reporting should be mandated, similar to what is expected in the UK. The report also recommends the creation of an anti-slavery commissioner.

The 2023 Canadian law is modeled after the three laws mentioned above, with the crucial difference that it requires companies to report the actions they have taken to mitigate both forced labor and child labor. The reporting requirements are similar, however. A major difference is that if companies are found to be in violation of the law, they could face conviction and fines of up


to 250,000 Canadian dollars. These differences give the Canadian act more teeth than the other acts, but it is too early to gauge its effectiveness. The first set of reports on its outcomes are not due until 2024.

Comprehensive European Legislations on Labor and Environmental Standards in Supply Chains

Over the last five years, there has been a flurry of legislative activity in Europe that seeks to mandate due diligence on supply chains with stringent reporting requirements that will potentially hold companies more accountable for negative impacts on both the environment and labor issues. The earliest piece of legislation was the French Corporate Duty of Vigilance Law, enacted in 2017, that requires any corporation established in France with five thousand or more employees in France and ten thousand or more worldwide to create a vigilance plan for labor and environment issues in their supply chains. The plan must identify and rank potential risks, outline procedures to periodically assess subcontractor and supplier compliance, outline steps to address risk and remedy violations, document a method for identifying risks in cooperation with relevant trade unions, and establish a monitoring system to assess the effectiveness of the program. If companies fail to comply with the formal notice of violations within three months, they may be required to comply by way of a court order at the request of any person having an interest in bringing proceedings to court. Moreover, the court may order the company to pay a civil penalty determined in relation to the seriousness of the alleged misconduct but not exceeding ten million euros. This civil penalty cannot be deducted from the taxable income of the company.

At the time of writing, there are several cases pending before the French courts. For example, NGOs have sued the bank BNP Paribas for supporting fossil fuel companies that have negative climate impacts. The lawsuit alleges that the bank’s loans to big oil and gas companies breach the bank’s duty of vigilance to not harm the environment. Similar complaints have been made against food company Danone for its use of plastic and Casino for purchasing meat from suppliers who are engaged in deforestation of the Amazon and land-grabbing from Indigenous peoples. The first case decided by the French courts was that of Total Energies, a French oil company sued by NGOs for

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violation of the vigilance law in relation to the environmental damage caused by its oil exploration activities in Uganda and Tanzania. On February 28, 2023, the French court dismissed the claims on procedural grounds—that it was sued in the wrong court and the requirement of a formal notice was not complied with. Other decisions, however, are pending. The French law is unique in that it allows suits to be brought against a company for violation of its duty of vigilance, and it does not restrict or clarify who can bring suits. Although the suits filed thus far in France only relate to environmental issues, labor issues could be addressed similarly.

Most recently, and in the same vein, Germany has adopted the Act on Corporate Due Diligence Obligations in Supply Chains, which entered into force on January 1, 2023. Commonly called the Supply Chains Due Diligence Act, the legislation imposes due diligence obligations on enterprises to comply with environmental and human rights standards in their supply chains. The law applies initially to enterprises based in Germany with more than three thousand employees and German-registered branches of foreign companies with over three thousand employees. In the second phase, beginning in January 2024, the law’s scope will be broadened to include enterprises based in Germany or German-registered branches of foreign companies employing over one thousand employees. About 2,900 companies will fall under this law. Companies must publish an annual report on the fulfilment of their due diligence obligations. For most companies subject to the act as of January 2023, the first report will be due in April 2024 at the latest. According to the law, the report must include specific information on the identified human rights and environmental risks under the law, the company’s efforts to fulfill its due diligence obligations, and how the company assesses these efforts and their impact, as well as what conclusions it draws from this assessment for the risk management system and future due diligence measures. The Federal Ministry for Economic Affairs and Export Control has developed a questionnaire that firms can use to report these issues.

The German law differs from the French law in two major respects. First, it puts greater emphasis on labor issues than on environmental issues. Second, it does not envisage that aggrieved parties in the wider supply chain can sue in German courts; rather, the ministry will rely on administrative

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enforcement through inspection of the reports. Noncompliant companies can face fines up to 2% of annual revenues and exclusion from public tenders for up to three years.

**EU Legislative Initiatives**

There are two due diligence legislative initiatives at the EU level. Both have gone through the legislative process and have been approved by the European Commission, Council of Ministers, and parliament. These are the Corporate Sustainability Reporting Directive (CSRD) and the Corporate Sustainability Due Diligence Directive (CSDDD).

The CSRD entered into force on January 1, 2023. It builds on several pieces of earlier EU legislation requiring financial and nonfinancial reporting requirements for EU companies. The directive requires large companies (those with more than 250 employees) to disclose information regarding how they identify, manage, and mitigate sustainability risks and the potential impact on business strategies and financial performance. The reporting requirement includes environmental issues (e.g., climate change, biodiversity), social issues (e.g., labor and human rights, diversity), and governance issues (e.g., corruption, tax transparency). The law covers companies’ own workforces as well as those of suppliers. The key purpose of the legislation is to provide investors and stakeholders with relevant, reliable, and comparable information on the sustainability performance and impact of companies. The CSRD does not yet provide clear guidance on how to determine what is material or which issues should be disclosed. There remains an element of uncertainty, therefore, that needs to be clarified. Given that the law is now in force, I would expect clarification to be issued shortly.

The CSDDD was first published by the European Commission in February 2022. The European Council adopted its position on this directive on December 1, 2022, and the European Parliament passed a slightly more stringent version in June 2023. The final version of the law will result from negotiations between these three European institutions. Once these

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negotiations are complete, European states will have two years to “transpose” the directive into their own national legislation. The overall purpose of this directive is to have a European regulatory framework on human rights and sustainability due diligence and establish consistency with other EU directives such as the CSRD. The CSDDD aims to introduce a comprehensive framework to identify actual and potential risks to human rights and the environment and to outline plans to mitigate those risks. The law applies to companies, their subsidiaries, their suppliers, and other organizations within their chain of activities.

At the time of writing, the three EU institutions have not yet resolved their differences on the CSDDD. There are disagreements about the scope of coverage (the turnover and employee count thresholds), the applicability to financial service companies, the scope of the value chain, the types of adverse human rights and environmental impacts, the penalties for noncompliance (which are generally left to member states), and, perhaps most importantly, the liability for civil damages. If companies covered by the legislation can be sued in EU courts by those adversely affected by violations of human rights and environmental issues in their supply chains, it could be a game-changer for international regulation.

CONCLUSION

The outlook for the regulation of labor conditions is still unclear. Much depends on how stringent the CSRD reporting requirements are and how the CSDDD will hold companies accountable for their actions across their value chains. On the one hand, there is the possibility that the reporting requirements under both laws will focus on descriptions of corporate policies regarding human rights and environmental risks and less on the impact of those policies. This would allow for decoupling, where companies are evaluated on their policies but not on those policies’ outcomes. This currently appears likely in respect to the CSRD. But if the CSDDD allows companies to be sued in European courts for labor violations in their value chains, the legislation could have major ramifications for the entire value chain ecosystem of each covered European corporation. If a stringent version of CSDDD accountability is introduced, there would be broad implications for different actors in global apparel.

Global apparel companies will need to get more serious about ensuring that they mitigate risks related to human rights and environmental issues in their supply chains. This may involve, for example, developing stable
relationships with suppliers and paying suppliers more for their products to improve working conditions in factories.

Global companies will also demand more from their auditors since social auditing is the primary source of information that companies have regarding practices in their suppliers’ factories. Social auditing will need to be improved significantly, which means companies must start paying their auditors instead of having their suppliers pay them. And these firms must pay their auditors more appropriately so that the audits go beyond the “tick the box” exercise that they currently are.

Apparel-exporting countries, especially those whose competitive advantage thus far has been cheap costs and low regulatory standards, will need to ratchet up their human rights and environmental enforcement, given that global companies will now be looking to source from locations where there are fewer human rights and environmental risks. This will be especially true for countries that are nearly wholly dependent on apparel exports for their economic development, such as Bangladesh and Cambodia, but also for all countries where low costs and lax regulation have been important drivers for foreign investment, such as Vietnam, Indonesia, and India. Asian countries have long followed export-oriented industrialization strategies, leveraging their lower costs and light-touch regulation.

Similarly, suppliers in these countries may also be induced to follow higher-road employment practices. At the time of writing, Bangladeshi garment workers are striking and rioting, unhappy that the minimum wage increase proposed by employers and the government does not even cover the costs of inflation. Since paying an adequate wage is one element in most corporate sustainability programs, global brands may need to help suppliers raise wages by paying higher prices for their products.

In sum, we are at a crossroads in terms of human rights, labor, and environmental regulation transnationally. Although the private-regulation efforts of the past 20–30 years have possibly had some positive impact, they are too piecemeal, opaque, and weakly enforced to significantly change worker rights in the apparel industry. Stricter government regulation may be required to ensure that global brands are actively addressing these issues in their supply chains, and the shape of European legislation will significantly influence the future of worker rights.