Legal Transplants through Private Contracting: Codes of Vendor Conduct in Global Supply Chains as an Example

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Legal Transplants through Private Contracting: Codes of Vendor Conduct in Global Supply Chains as an Example

The legal transplant literature typically focuses on legal transplants through governmental channels (e.g., legislative or judiciary processes). This Article, however, directs attention to a generally ignored phenomenon: legal transplants through private contracting in the globalization age. Private actors have transplanted a variety of private and public laws across jurisdictions through contracting for over a decade. This Article argues that codes of vendor conduct in global supply chains are a vivid example of this type of legal transplantation. Given that these vendor codes can be interpreted as legal transplants through private contracting, this Article further examines the transplant effects in China, one of the many receiving countries. Finally, this Article proffers a theoretical analysis of the comparative advantages and disadvantages of legal transplants through private contracting.

I. INTRODUCTION

The history of legal transplants can be traced back thousands of years. An early wave of large-scale legal transplants was driven by colonialism. Legal transplants could be viewed as a tool for colonists to control their new settlements. In the post-World War II period, a large number of newly independent states borrowed laws from western countries. To a great extent, such borrowings still reflected the legacy of colonialism. The legal transplants during the colonial and the post-World War II periods tended to be blanket transplants of a certain legal system, which facilitated the formation of legal families. In the late 1980s, the legal reforms of former socialist countries initiated another wave of legal transplants. More recently, global

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economic integration has become a powerful engine pushing the wave of legal transplants to its apex.

In the era of globalization, legal reforms at the individual state level usually transfer fragments of rules from various legal systems and integrate the fragments into a single law. The concept of legal families that may be deemed a colonial legacy is expected to diminish. A parallel idea to the combination of fragmented rules from different foreign sources into a single law in a national legal reform is the legal standardization or harmonization, particularly in the global finance and trade arena. International governmental, semi-governmental, and non-governmental organizations (NGOs) are the major contributors to legal standardization and harmonization today. At present, there are hard and soft approaches to facilitate that goal. The hard approach is notably illustrated by the legal interactions between the WTO and its members, or between the EU and its Member States. The soft approach can be seen in examples such as OECD Corporate Governance Principles, UNCITRAL Model Law on International Commercial Arbitration, and UNIDROIT Principles of International Commercial Contracts. The impetus behind these projects is to reduce transaction costs for international market participants as well as the hope to improve the institutional environments of receiving countries. The transplanted laws under the standardization or harmonization movement are usually products of international negotiation and conciliation, rather than wholesale adoptions of any particular legal system. For example, the OECD Principles on Corporate Governance contain elements of the Anglo-American shareholder model and the European stakeholder model. States generally play a key role in this transplant process because the standardized rules are made by states at the international level, and the laws usually need to be incorporated into a legal system through legislative processes at the national level. Given that standardized or harmonized laws are usually mixtures of different legal sources, every country, whether developed or developing, subject to these laws may treat them as legal transplants to a certain extent. However, the transplant aspect tends to be more striking for


3. Legal standardization and harmonization cover a wide range of approaches with variations of coerciveness: legally-binding agreements backed by enforcement mechanisms, economic enticement, non-binding principles intended to provide guidance, and foreign technical assistance programs. The hard approach refers to measures backed by legal enforcement, while the soft approach refers to measures not backed by legal enforcement.

4. Developed countries may treat harmonized laws as legal transplants, see e.g., Gunther Teubner, Legal Irritants: Good Faith in British Law or How Unifying Law Ends Up in New Divergences, 61 Mod. L. Rev. 11 (1998) (analyzing the transplant of the European continental principle of bona fides into the British contract law through the EU Directive on Unfair Terms in Consumer Contracts).
developing countries because they usually have a weak voice in the international lawmaking process and relatively limited development of their legal institutions. Some scholars caution against the possible dangers of overzealous legal standardization and harmonization to developing countries. The potential dangers of legal standardization and harmonization to developing countries. Professor Katharina Pistor in particular envisions the potentially harmful effects resulting from ignorance of the interdependence of legal rules embedded in a legal system and the adaptation process operated by local law users.

According to contemporary legal transplant scholarship, the state (the governmental organs, particularly the legislative branch) is the major conveyor of foreign law, holding the power over whether and how to transplant. The transplanted objects are usually formal law codified in a legal system. The transplant motivations are normally associated with political or governmental functions, such as regulating a new national problem, pursuing foreign policy interests, or gaining governmental legitimacy.

A much less noticed phenomenon occurring in the globalization age is that law can be transplanted by non-state actors. Some non-state actors also play an important transplant role in the legal standardization and harmonization movement. For example, the International Accounting Standards Board (IASB), a non-profit, private sector organization, develops international standards for financial reporting; the International Organization of Securities Commissions (IOSCO), which includes public and private securities regulators, develops international principles of securities regulation. But these non-state actors usually still follow the typical transplant method, which involves government legislation/regulation processes at the national level. This Article discusses another type of legal transplants through private actors: borrowing law through private contracting. Through the channel of contracting, private transactors have been "smuggling" tons of regulatory law across borders for over

6. See Pistor, supra note 5.
a decade. This phenomenon is rarely detected by the radar of legal transplantation. The purpose of this Article is to direct attention to this specific type of legal transplantation.

International commercial arbitration may be put into this category. Arbitration as a dispute resolution mechanism is increasingly popular with international commercial actors. By virtue of arbitration or through choice of law clauses in private contracts, foreign legal rules that would be otherwise inapplicable may be contractually transmitted in a given dispute. An advantage of arbitration is that it can largely, though not completely, circumvent local legal institutions that are incapable of delivering acceptable adjudicatory outcomes to the contracting parties. This is an important advantage, especially for contracts to be enforced in countries where rule of law is weak or lacking. Professor Inga Markovits names this kind of legal transplantation “the potted transplant”: “self-contained organisms that carry their own foundation and substance with them and that, like a houseplant, can be placed anywhere the purchaser desires (and the light is right).” The potted transplant is a form of “private ordering as an alternative to public law reform.” Note that although arbitration law appears neutral in that it gives contracting parties great latitude regarding their choice of procedural and substantive rules, the international arbitration practices between western and nonwestern transactors usually show a tendency toward westernization. This makes the legal transplant feature of international arbitration more prominent in the eyes of nonwestern parties.

This Article proffers another example of legal transplants via private contracting: multinational companies’ codes of vendor conduct in their global procurement contracts. Codes of vendor conduct refer to a set of supplier eligibility criteria structured with social and environmental standards established internally by a buyer company itself or externally by NGOs; they are usually accompanied by an internal or external auditing system. Examples of such codes of vendor

9. The reason why it is not a complete circumvention is that if a contracting party does not voluntarily comply with an arbitration award, the other party may seek enforcement by local courts. When the award is to be enforced by local courts, the quality of local legal institutions affects contract enforcement. See Randall Peerenboom, Seek Truth From Facts: An Empirical Study of Enforcement of Arbitration Awards in the PRC, 49 Am. J. Comp. L. 249 (2001) (using the enforcement of arbitration awards by the Chinese courts to test the development of rule of law in China); Daniel Berkowitz et al., Legal Institutions and International Trade Flows, 26 Mich. J. Int’l L. 163 (2004) (arguing that domestic institutions remain important in the global trade because global traders still rely on local legal systems when contracts or arbitration awards are not voluntarily complied; based on the incomplete contract theory, complex goods exporters suffer more when the local legal institutions are weak).


11. See id.

conduct in global supply chains include the Gap Code of Vendor Conduct, Wal-Mart Standards for Vendor Partners, HP Supplier Code of Conduct, and many corporations’ procurement policies that refer to standards such as SA8000 or ISO 14001. Although a great body of literature on global labor and environmental governance discusses at length the potential and limitations of such private codes as a transnational and nongovernmental regulatory mechanism, no study has yet looked at the codes from a legal transplant perspective. Therefore, a major purpose of this Article is to explain how the private codes in global commerce can be interpreted as a form of legal transplantation through private contracting.

Currently, a large and growing number of multinational companies adopt codes of vendor conduct into their supplier selection requirements. At first glance, the proliferation of such codes running through global supply chains and getting to developing countries may simply be deemed a replication and transmission of business strategies between corporations, which are a result of private economic competition. The typical notion of legal transplantation, which contains sovereignty and legitimacy elements, seems irrelevant to the proliferation of such business practices. But the underlying configuration of business transactions in global supply chains is more complex than that. As this Article shows, multinational companies transform international as well as their home-country laws into concrete legal obligations by contracting with companies in developing countries. Although it is well-known that many business strategies have been turned into contractual obligations, in the eyes of suppliers especially in developing countries, codes of vendor conduct have regulatory features that other business strategies do not possess. From the perspective of these suppliers, the regulatory features of vendor codes derive from the combination of the following arrangements: a contractual obligation of implementing the social and environmental

standards that used to be within the sphere of public regulation; the
designated contract enforcement mechanisms that are independent
from weak legal institutions in many developing countries, and; the
sanction of losing business, which is ultimately judged by multina-
tional companies.

The thesis in this Article is that multinational companies,
backed by their strong bargaining power, have transmitted a new le-
gal order to developing countries through contracting with local
suppliers and that such transmission may be interpreted as a form of
legal transplantation. This kind of legal transplantation is different
from the usual type in several aspects. First, it is multinational com-
panies (non-state actors) rather than states playing a key role in the
transplant process. Multinational companies' strong bargaining
power as the source of authority and non-legal institutions as con-
tract enforcement mechanisms make the transplants possible.
Second, the vendor codes themselves are not government-mandated
laws. Yet, they have an effect of approximately reflecting interna-
tional law or multinational companies' home-country law or even the
already transplanted but poorly enforced law in receiving countries.
Third, this kind of transplantation is a response primarily to market
demands rather than to political considerations. Economic and social
pressures in the multinational companies' home countries are the ul-
timate forces behind this type of legal transplantation.

When a law is transplanted from one state to another, the viabil-
ity of the law in the new environment depends on numerous factors
external to the quality of the transplanted law itself. Basically, the
outcome of a legal transplant can be mutation, withering, or, albeit
rarely, unscathed survival. Looking at vendor codes in global supply
chains as a form of legal transplantation raises the question of what
the results of such legal transplants are. Since vendor codes in global
supply chains are mainly implemented at factories in developing
countries, this Article takes China, characterized as "the world's fac-
tory," as a case study. China provides interesting perspectives on the
circumstances under which vendor codes in global supply chains can
be easily assimilated into a receiving country and on the extent to
which the legal transplants may be regarded as successful in terms of
the intended purposes.

As Alan Watson argues, human history is full of works recording
the importance of legal transplants in the development of law. 14
Globalization unquestionably makes these works much more conspic-
uous than ever. The revolution of manufacturing modes in the
globalization age has brought about innovations in legal transplant
methods. More research is necessary to examine the various kinds of
legal transplant methods and to compare their advantages and disad-

14. See generally WATSON, supra note 1.
vantages in different settings. This Article draws attention to these issues which are of increasing importance in the globalization age. Such a study is important and useful for international and national policymakers when making legal reforms.

This Article is arranged as follows: Section I explains why vendor codes in global supply chains can be interpreted as a form of legal transplantation through private contracting. It considers the transplant motivation, objects, and process. Based on the understanding that vendor codes in global supply chains are legal transplants, Section III takes China, a major receiving country, as a case study to illustrate how the transplanted legal order interacts with the local environments. This Article particularly compares the different results of the imported social and environmental standards, i.e., SA8000 and ISO 14001. Section IV proffers some theoretical contributions to the literature on legal transplantation.

II. THE BASIC STRUCTURE OF VENDOR CODES IN GLOBAL SUPPLY CHAINS AS LEGAL TRANSPLANTS

Although there are a large number of academic studies examining vendor codes in global supply chains, none considers the vendor codes as legal transplants. Therefore, it is important to explain why vendor codes in global procurement contracts square with the concept of legal transplantation through private contracting. To illustrate the structure of the vendor codes as legal transplants through private contacting, this section analyzes the transplant motivation, objects, and process.

A. The Transplant Motivation

Codes of vendor conduct require suppliers to meet certain labor and environmental protection standards in the production process. The labor standards generally include topics concerning child labor, forced labor, health and safety measures in workplaces, freedom of association and right to collective bargaining, discrimination, working hours, and compensation. The environmental standards usually involve hazardous substance management (e.g., safe handling, shipping, storage, recycling, and disposal of hazardous materials), waste management, air emission management, energy efficiency measures, and other pollution prevention requirements.

But why do multinational companies require suppliers to meet labor and environmental standards in the production process? These standards seem irrelevant to the tangible quality of products themselves. The answer to the question has social, economic, and business management aspects.

The social aspect relates to the changes in consumer expectation in developed markets. Prior to globalization, companies only ran a
race with domestic competitors who were subject to the same cost basis and regulatory environment. In the globalization age, however, the competition is ruthless, pushing every company to compete regardless of its size, origin, and industry. In order to survive in the competitive global market, companies have adopted new business management methods, one of which is to reshape supply chains for cost reduction. An important aspect of the reshaping is the extension of supply sources from domestic to global, particularly in order to tap into the reservoir of cheap labor and natural resources in developing countries. The supply manufacturers in developing countries that contract with multinational businesses are usually companies that are small when measured on an international scale. These small manufacturers profit from the multinationals’ cost-reduction strategy. They make profits not from selling advanced knowledge, but from selling cheap labor and materials. To be competitive and profitable, these suppliers do not pay much attention to labor and environmental protection concerns and sometimes even egregiously violate laws, gaining profits at the expense of workers’ health and local environments. Moreover, the regulatory institutions in developing countries are usually incapable, or unwilling because of the national comparative advantage concern, to control these harmful practices. Meanwhile, product competition in developed markets has become so fierce that multinational companies are pressed to squeeze every penny out of their operations, including their supply chains. Therefore, multinational companies do not have strong incentives to consider the production processes of their suppliers in developing countries. Price is their primary, if not only, concern. Workers and environments in developing countries suffer in this unregulated global supply chain. Since the 1990s, a large number of news reports have revealed multinational companies’ massive labor exploitation and environmental destruction in developing countries. The revelations of corporate irresponsibility have caused consumers and NGOs in developed markets to boycott the companies and to initiate the movement of corporate social responsibility (CSR). The CSR movement signals that corporations are expected not only to provide goods, services, and employment, but also to undertake social and environmental obligations in proportion to their economic power. Codes of vendor conduct in global supply chains constitute an important

15. See, e.g., Philip Shenon, Made in the U.S.A.? — Hard Labor on a Pacific Island/A Special Report.; Saipan Sweatshops Are No American Dream, N.Y. TIMES, July 18, 1993, § 1, at 1 (reporting that labor exploitations were found in the suppliers of Arrow, Liz Claiborne, Gap, Montgomery Ward, Geoffrey Beene, Eddie Bauer, and Levi-Strauss).

16. For the anti-sweatshop movement since 1990s, see KIMBERLY ANN ELLIOTT & RICHARD B. FREEMAN, CAN LABOR STANDARDS IMPROVE UNDER GLOBALIZATION? 147-50 (2003) (including a timeline of anti-sweatshop activities in the 1990s).
branch of the CSR movement. They are a response to social change, and social change has practical economic and business significance.

In economic terms, although outsourcing to suppliers in developing countries where cheap labor and loose regulatory control can reduce certain costs, it does not guarantee reduction in total production costs. In economic parlance, "the costs of production are the sum of transformation costs and transaction costs." Global outsourcing may reduce transformation costs (e.g., labor wages); however, it may also increase transaction costs. The transaction costs including how to control the quality of production processes (including labor and environmental conditions) would be very likely to surge given that the exchanges are between parties in markets with great distance in space, business culture, and institutions. Therefore, it is important to ensure that, for a profitable outsourcing, if there is any increase in transaction costs, such increase would not eliminate the benefits derived from reduction in transformation costs.

In business terms, it is a question about supply chain management—how to manage risks in the lengthened supply chains. Since companies do not have direct control over their suppliers’ factories, the core mission of supply chain management is to ensure the smooth flow of supply. Price, delivery speed, quality, and reliability are the typical focuses of supply chain management. From a multinational company's standpoint, there are multiple layers of suppliers, from its first-tier suppliers, with which it has direct relationships, to its suppliers' suppliers with which it has no contact at all. Multinational buyers may very well argue that they are incapable of controlling their suppliers, in particular those hidden under the multiple layers of contracting. Ostensibly, the shift of manufacturing to suppliers in developing countries and the invisibility of suppliers may justify shifting labor and environmental protection costs associated with manufacturing processes to the suppliers. This is an important economic reason for multinational buyers to extensively utilize suppliers in developing countries. However, sweatshop practices and adverse environmental impacts hidden in the extended and entangled supply chains and traced back to multinational companies have become increasingly known throughout the world. This has brought a deluge of condemnation by consumers in their major markets. This indicates that supply chain management must obtain not only high quality products with low prices by timely delivery but also do so in a socially and environmentally responsible manner.

In short, multinational companies adopt codes of vendor conduct in their global supply chains because of social and economic pressures in their major markets. Codes of vendor conduct in global supply

chains are a tool to satisfy social demands and to control transaction costs and risks arising from socially or environmentally irresponsible conduct by their suppliers. The transplant motivation is driven by multinational companies' enlightened self-interest—responsively to repair their tarnished images, or preventively to maintain customer goodwill.\textsuperscript{18}

B. The Transplanted Law

By reviewing codes of vendor conduct in global supply chains, it is easy to find that the contents of such codes usually refer to three categories of legal texts: international law, the multinational company's home-country law, and the supplier's country law. The former two types agree with the notion of legal transplantation. The scope of "international law" in this section includes hard and soft law. The distinction between them lies in whether the law can be enforced by formal legal sanction, though sometimes it may be proper to interpret the relationship between hard and soft law as a spectrum rather than a dichotomy.\textsuperscript{19}

With regard to social standards, codes of vendor conduct frequently refer to International Labor Organization (ILO) Labor Conventions, the Universal Declaration of Human Rights, and the UN Convention on the Rights of the Child.\textsuperscript{20} These international conventions and declarations aim at setting up internationally minimum labor standards. One may argue that vendor codes citing these international laws cannot be treated as legal transplants because many developing countries have already signed and ratified these international laws. This argument is true only to a limited extent. A large number of vendor codes refer to the ILO conventions on hours of work and freedom of association, but these conventions are not ratified by

\textsuperscript{18} See, e.g., Robert J. Liubicic, Corporate Codes of Conduct and Product Labeling Schemes: The Limits and Possibilities of Promoting International Labor Rights Through Private Initiatives, 30 LAW & POL'Y INT'L BUS 111, 114-15 (1998) (arguing that self-interest motivation is the predominant reason multinational companies adopt codes of conduct); Harvey L. Pitt & Karl A. Groskaufmanis, Minimizing Corporate Civil and Criminal Liability: A Second Look at Corporate Codes of Conduct, 78 GEO. L.J. 1559, 1573-1600 (1990) (providing a historical review of the growth of codes of conducts fostered by scandals); Murphy, supra note 13, at 397-403 (explaining the impetus for the proliferation of codes of conduct); ELLIOTT & FREEMAN, supra note 16, 42-46 (2003) (describing firms' practice of adopting codes of conduct because they believe that "consumers will penalize them if they do not undertake corrective action" and analyzing firms' cost-benefit calculation of adopting higher labor standards).


major exporting countries such as Brazil, China, and Thailand. More importantly, signatory states may not actually implement these international conventions at the national level. According to the orthodoxy of international law, these laws have no direct application to corporations and individuals when the state is not a signatory or when the state is a signatory but does not incorporate the respective conventions into domestic law. Therefore, when international labor law is incorporated into vendor codes and further transformed into contractual obligations, it can be deemed a direct application of international law to private entities in developing countries.

In addition to the reference to the international legal instruments of which states are the addressees, codes of vendor conduct also consult international instruments that target corporations, such as the UN Global Compact. The contents of these standards usually link back to the ILO conventions and UN declarations previously mentioned.

With regard to environmental issues, frequent references include the ISO 14001 Environmental Management System and the EU Eco-Management and Audit Scheme (EMAS). In contrast to the international labor standards dictating substantive requirements, the international environmental instruments referred to in the codes of conduct are procedural rules. They offer standardized environmental management process and auditing principles. Vendor codes in global supply chains therefore transplant the internationally-standardized environmental procedural rules.

Codes of vendor conduct also incorporate multinational companies' home-country laws. When a multinational company adopts a set of universal standards for its worldwide operations, the multinational company's home-country law is an important reference. An explicit example can be seen in the code of vendor conduct of New

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21. For example, major developing countries that export labor-intensive products, such as Brazil, China, Thailand, Malaysia, and Vietnam do not ratify Convention 1 (hours of work for industry) and Convention 87 (freedom of association). India does not ratify Convention 87. Indonesia and Russia do not ratify Convention 1. See International Labour Organization Database of International Labour Standards Country Profiles, at http://www.ilo.org/ilolex/english/newcountryframeE.htm (last visited Sept. 3, 2007).


23. The UN Global Compact is an international initiative with an objective to promote corporate social responsibility and to advance ten universal principles in the areas of human rights, labor, environments, and anti-corruption. See www.unglobalcompact.org/.

24. For detailed discussion about ISO 14000, see Section III of this Article. The EU Eco-Management and Audit Scheme (EMAS) is a management tool for companies and other organizations to evaluate, report, and improve their environmental performance. For more information, see http://ec.europa.eu/environment/emas/index_en.htm (last visited Sept. 3, 2007).
Balance, a U.S.-based branded athletic shoe company. In New Balance's Supplier Code of Conduct, the safety and sanitary conditions of workplaces are measured against the benchmark set by the United States Occupational Safety and Health Administration (OSHA). Nike, a U.S.-based branded sportswear giant, also requires its footwear suppliers to provide indoor air quality equal to or better than the limits established by U.S. OSHA.

The standards set forth in codes of vendor conduct may differ from applicable laws in countries where suppliers operate their factories. A typical resolution to the conflict is to choose the stricter standard. Therefore, foreign law (including international law and multinational companies' home-country law) adopted by codes of vendor conduct may actually control a given labor or environmental issue.

Note that the transplanted law here is public law and regulatory in nature. Part of the transplanted law involves human rights such as freedom of association and prohibition on forced labor. This is an important point that we should bear in mind, given that business and commercial laws are generally assumed more easily to transplant than human rights law because of the differences in their institutional sensitivity. This nature of the transplanted law may significantly affect transplant outcomes.

C. The Transplant Process

1. Private Contracting

Codes of vendor conduct are real legal obligations in global supply contracts. Although supply contracts are usually confidential and not accessible to the public, publicly available information, such as corporate statements posted on companies' websites and material contracts filed with SEC, has demonstrated the prevalence of codes of vendor conduct as contractual obligations. Professor Michael Vandenbergh recently conducted a study concerning the pervasiveness of environmental standards in the procurement policies of the

27. See, e.g., Article II of SA8000, available at http://www.sa-intl.org/; the Ethical Trading Initiative Base Code, http://www.ethicaltrade.org/Z/lib/base/code_en.shtml; Nike Code of Conduct (e.g., hours of work/overtime); IBM Supplier Conduct Principles (e.g., child labor, working hours, etc.).
28. See Frederick Schauer, The Politics and Incentives of Legal Transplantation, (Center for International Development at Harvard University, Working Paper No. 44, Apr. 2000) (arguing that "political, social, and cultural factors are more important in determining the patterns of legal migration for constitutional and human rights laws, ideas, and institutions than they are for business, commercial and economic laws, ideas, and institutions").
top ten companies in various sectors as identified by Hoovers, a Dun & Bradstreet affiliate. He found that, based on the policies and statements disclosed by the companies themselves, at least half of the top ten companies in various sectors have imposed some type of environmental requirements on their suppliers. He also found that eleven of the fifty-two supply agreements (21%) filed with the SEC during the fourth quarter of 2001 include environmental requirements for suppliers, and some of the environmental standards imposed are not even required by the environmental law in the suppliers’ countries.

According to the information found with the phrases “code of vendor conduct” and “supplier code of conduct” in the LexisNexis SEC EDGARPlus Exhibits database, a number of companies such as Tommy Hilfiger, a premium apparel company, also include labor standards (e.g., SA8000) in the contracts with their suppliers. Hewlett-Packard, a well-known computer equipment company, openly discloses its standard contract concerning HP’s code of vendor conduct on its corporate website. The contract is called “the Supplier Social and Environmental Responsibility Agreement,” which requires all of its suppliers to sign the agreement and comply with HP’s supplier code of conduct.

2. Contract Enforcement

Contract enforcement plays an important role in the legal transplant process. Legal scholarship commonly finds gaps between the law on the books and the law in practice after transplants. Codes of vendor conduct confront the same problem. Multinational companies such as Nike, Gap, and Wal-Mart, provide vivid case examples showing that simply transforming codes of vendor conduct into contractual obligations does not warrant compliance by suppliers in developing countries. Therefore, how to ensure that suppliers actually respect


30. See, e.g., Tommy Hilfiger Corp. (Form 10-K, Exhibit 10. Material Contracts, filed on June 26, 2001), Phoenix Footwear Group Inc. (Form 10-Q, Exhibit 10. Material Contracts, filed on Nov. 15, 2005), Stride Rite Corp. (Form 10-K, Exhibit 10. Material Contracts, filed on Mar. 1, 2000), Marvel Entertainment Group Inc. (Form 10-Q, Exhibit 10. Material Contracts, filed on Aug. 21 1998). This author does not argue that the information found here was complete.


32. Nike established the code of conduct for its suppliers in 1992, but in the late 1990s, Nike was seriously charged for its suppliers’ labor exploitation despite the code’s existence. The famous case is Kasky v. Nike Inc., 79 Cal. App. 4th 16; 27 Cal. 4th 939. Wal-Mart also adopts a code of conduct for its suppliers but is still infamous for its suppliers’ poor labor performance. See also Leslie Kaufman & David Gonzalez, Made in Squalor: Reform has Limits: Labor Standards Clash with Global Reality, N.Y. TIMES, Apr. 24, 2001, at A1 (reporting Gap intensified monitoring efforts because suppliers failed to comply with Gap’s code).
the social and environmental standards in the production process has been a challenging question for global buyers. A prevailing solution by global buyers is to use internal and external auditing systems to enforce the contractual obligations.

An internal audit is conducted by trained employee auditors of a buyer company. There is a trend, however, that global buyers are also using external auditing by specialist auditing firms or NGOs. The typical audit includes three main aspects: a physical inspection (a factory tour); interviews with employees; and a review of records concerning payroll, tax, insurance coverage, and environmental protection processes. Whether audits are announced or unannounced depends on different audit purposes and strategies. They are periodically conducted. After the audit, a report and corresponding corrective action plans are produced. The audited supplier would be given some time to correct identified problems.

There is an interesting question why global buyers use internal and external auditing to ensure suppliers' performance of the social and environmental obligations in global procurement contracts. Typically, there are three alternatives to enforce international commercial contracts, including formal procedures (i.e., in courts), informal mechanisms (e.g., reputation, networks, barter), and international arbitration. Based on this understanding, why do multinational companies favor internal and/or external auditing systems over the conventional enforcement mechanisms to enforce the social and environmental terms in supply contracts? This question may also be translated into a general inquiry of why state courts as a legal institution for dispute resolution are avoided and a new extra-legal enforcement institution is favored. The point of looking at the relationship between legal and extra-legal contract enforcement mechanisms is not to find systematic superiority of one over the other. Rather, scholars have recognized that each enforcement mechanism has its strengths and weaknesses for different kinds of transactions. Thus, we should examine each contract enforcement

33. For detailed discussion on the rise of such external auditing in the global supply chain and its theoretical implications, see Margaret M. Blair et al., The New Role for Assurance Services in Global Commerce, 33 J. CORP. L. 325 (2008).
34. For detailed discussion about how the audits are conducted, see e.g., Ivanka Mamic, Implementing Codes Of Conduct: How Businesses Manage Social Performance in Global Supply Chain 127-31, 202-20, 276-94 (2004); Jill Esbenshade, Monitoring Sweatshops 69-82 (2004); Nike, Inc., NIKE FY04 Corporate Social Responsibility Report (disclosing how Nike’s M inspection, SHAPE audit and FLA independent audit are conducted).
mechanism in the specific context of codes of vendor conduct in global supply chains; this will reveal the comparative advantages of using auditing systems.

Courts are not a favored enforcement institution because they have intrinsic and extrinsic limitations in the specific context of enforcing vendor codes. Although codes of vendor conduct adopted by multinational companies bear much resemblance to each other, the social and environmental standards are very industry- or even firm-specific.\(^\text{37}\) They vary depending on types of products, production procedures, and locations of factories. To determine whether a supplier's measures meet the standards set forth in the vendor code requires professional knowledge and experience. The standards in the vendor codes are more like regulations administered by labor and environmental agencies, which are somewhat outside courts' expertise. Moreover, disputes in courts over irresponsible outsourcing may attract public attention, and global buyers cannot easily disconnect themselves from the irresponsibility label attached by the public. This certainly spells trouble for their businesses. Global buyers prefer a way that they can retain confidentiality of production processes and have a chance to correct the problem before it becomes exposed to the public. Besides these inherent limitations, courts may not be available or reliable in many developing countries where suppliers mainly locate.

Global buyers may also turn to reputation to enforce the social and environmental standards in supply contracts. However, reputation as a contract enforcement mechanism is effective only under certain conditions.\(^\text{38}\) For example, reputation can work only where transactors can communicate the information accurately and inexpensively to other transactors in the business circle.\(^\text{39}\) Most of the pertinent scholarship builds on examples where certain ethnic ties, closely knit communities, and trade associations in certain industries facilitate the transmission of reputation information; such mechanisms are usually constrained by geography.\(^\text{40}\) However, buyers and

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\(^\text{39}\) See id. at 153.

\(^\text{40}\) See, e.g., Barak D. Richman, How Communities Create Economic Advantages: Jewish Diamond Merchants in New York, 31 LAW & SOC. INQUIRY 383 (2006) (arguing that the combination of family-based reputation mechanisms and community-based enforcement institutions allows the trading of valuable and portable articles); Lisa
suppliers in the complex global supply chains are generally on different continents and comprise different ethnic groups, languages, and business cultures. Also, reputation works well only when transactors have reputation at stake. Some small suppliers in developing countries may not take reputation seriously because the expectation of ongoing business relationships may be diminished by uncertainties in macroeconomic, political, and legal environments. Thus, reputation is a possible but not a sufficient enforcement mechanism in the specific content of vendor codes in global supply chains.

Arbitration seems to be a suitable enforcement mechanism for vendor codes in the supply chains given that it offers confidentiality, specialized substantive and procedural rules, and expert decision-makers. But arbitration involves situations where a dispute has already occurred. In other words, it is a remedial mechanism. Implementation of vendor codes, however, does not only have a remedial dimension but a preventive one. Since NGOs and media have shown their ability to peek into global buyers' supply factories, global buyers do not want to risk their reputation by solving problems ex post facto. In this regard, the typical arbitration model does not satisfy the prevention demand. To be sure, that does not mean arbitration plays no role in this transplant process. For example, when a buyer requires a supplier to be certified under SA8000 or ISO 14001 by an auditing firm, there is a contractual relationship between the audited party (usually a supplier) and the auditing firm. Disputes between the audited and the auditor concerning how to interpret and implement the contractual terms (including performance and auditing standards/measures) may still be subject to arbitration. 41 But this is a derivative question. This Article focuses on how to enforce vendor codes between a buyer and a supplier.

Thus, neither courts, nor reputation, nor arbitration provides a timely, proactive, and preventive solution to the compliance problem. Global buyers, therefore, resort to a tailored enforcement mechanism—internal and external auditing. Such auditing offers confidentiality, proactive monitoring, and preventive measures.


Internal and external auditing keeps production processes confidential and avoids unfavorable and uncontrollable exposure to the public. The information produced in internal auditing is not publicly accessible because the auditing process is conducted by the employees of a buyer for internal use. Unless the law mandates disclosure, the buyer can decide whether and how to disclose the information to the public, though the discretion has been challenged in recent years by the rising transparency demand from consumers and NGOs. For external auditing where a buyer uses outsiders, still only limited information is disclosed to the public. For example, when a company uses an auditing firm to ensure social and environmental performance, the auditing firm cannot disclose confidential information acquired in the audit without the consent of the audited.\footnote{See id. (confidentiality clauses in the contracts).}

Even NGOs that provide accreditation and/or certification services such as Worldwide Responsible Apparel Production (WRAP), Social Accountability International (SAI), and the member organizations of Standardization Organization International (ISO) disclose information only about applicant factories that pass audits but not those that fail.\footnote{The list of certified facilities released by WRAP can be found at http://www.wrapapparel.org/; WRAP even contains a statement: "We keep all information supplied by participating factories confidential unless instructed otherwise. Therefore, the list generated below contains only those factories that have provided express authorization to be mentioned. As such, not all WRAP certified factories in this country may be included." The list of certified factories released by SAI can be found at http://www.sa-intl.org/. ISO itself does not retain a list of certified facilities; it is the concern of organizations in each member country to provide such information. For example, China Quality Certification Center maintains a database to search certified facilities and check the validity of ISO 9000 and ISO 140000 certifications issued in China. See http://www.cqc.com.cn/Chinese/search/index.asp (last visited Sept. 3, 2007).} From the global buyers’ view, such confidential treatment helps to correct the enforcement problem without paying a reputational price.

In addition, internal and external auditing is conducted periodically and sometimes with no advance notice to suppliers. Periodic auditing and unannounced investigation are important for proactive and preventive purposes. This is because labor and environmental conditions can vary from moment to moment and may be temporarily fixed if a specific date for investigation is known in advance.

Finally, besides the comparative advantages of auditing, the role of external auditing in particular helps the operation of reputation as contract enforcement in the global market. The external auditing services providers, including auditing firms and NGOs, may be deemed reputation intermediaries facilitating the collection, verification, and dissemination of reputation information about suppliers’ social and environmental performance to global buyers.\footnote{See Blair et al., supra note 33.}
3. Imbalance of Power

In the transplant process, it is important to consider the relationship between the donors (multinational companies/global buyers based in developed countries) and the receivers (suppliers, particularly in developing countries). Based on the assumption that a contract is a result of negotiation, what are the dynamics in the negotiation process? In order to protect their corporate images, multinational companies require suppliers to comply with codes of vendor conduct. If the implementation of vendor codes is a gain without cost for both parties, there is no question that both sides (buyers and suppliers) would agree to incorporate the codes into contracts without any bitter discussion. Implementation of such codes, however, entails a non-negligible increase in production costs. For example, enhanced standards in wages, working hours, and working conditions would certainly raise production costs. Therefore, whether to adopt social and environmental standards into contracts and who should be responsible for the implementation are contested between buyers and suppliers, as these questions involve allocation of costs and benefits between the parties.

Power is an important factor influencing the outcome of the battle. As recognized in the business and sociological literature, power is an influential factor in defining the inter-firm relationships in supply chains. These structures are rarely balanced and may vary in different types of supply chains. Suppliers in developing countries usually have weaker bargaining power than multinational companies based in developed countries. This is particularly true for suppliers in apparel, footwear, toy, and other industries, in which codes of vendor conduct are very common. These industries are classic examples of buyer-driven commodity chains. "Buyer-driven commodity chains refer to those industries in which large retailers, branded marketers, and branded manufacturers play the pivotal roles in setting up de-

45. A number of early research articles on marketing channels have examined the power relationships between firms. See, e.g., Shelby D. Hunt & John R. Nevin, Power in Channels of Distribution: Sources and Consequences, 11 J. Mktg. Res. 186 (1974); Jack Kasulis & Robert E. Spekman, A Framework of the Use of Power, 14 Eur. J. Mktg. 180 (1980). The research specifically on the power factor in the supply chain is of more recent vintage. See, e.g., Michael Maloli & W.C. Benton, Power Influences in the Supply Chain, 21 J. Bus. Logist. 49 (2000). These studies primarily develop on the typology of social power proposed by French and Raven. See John R.P. French, Jr. & Bertram Raven, The Bases of Social Power, in STUDIES IN SOCIAL POWER 150-65 (Dorwin Cartwright ed., 1959). French and Raven propose five types of social power: reward, coercive (ability to punish), legitimate (a person internalizes values because of an obligation to accept the external influence, e.g., power from cultural values, social structure), referent (a person desires association with another person, a role or a group), and expert (knowledge and information). Another important idea related to the role of power between firms is the resource dependence theory proposed by Pfeffer and Salancik. See Jeffrey Pfeffer & Gerald R. Salancik, THE EXTERNAL CONTROL OF ORGANIZATIONS (2003).
centralized production networks in a variety of exporting countries,” particularly developing counties. Profits in the buyer-driven chains are gained from the “unique combination of high value research, design, sales, marketing and financial services that allow the retailers, branded marketers and branded manufacturers to act as strategic brokers in linking overseas factories with evolving product niches in the main consumer markets.” With the power to shape consumer demand in markets through the use of brand names and strategic networks, the buyers (retailers, branded marketers, and branded manufacturers) have leverage in price bargaining with suppliers and in setting business conditions (e.g., vendor codes) with suppliers in developing countries. Although a global buyer with strong bargaining power may have good reasons to forgo the use of power and share gains from a cooperative relationship with its suppliers, practical experience in developing countries suggests that global buyers in buyer-driven commodity chains tend to maximize their bargaining power over suppliers when inserting codes of vendor conduct in supply relationships.

In other words, from the view of suppliers in developing countries, codes of vendor conduct in global supply contracts match the externally-dictated transplant under Professor Jonathan Miller’s typology of legal transplants. The externally-dictated transplant involves “a foreign individual, entity or government that indicates the adoption of a foreign legal model as a condition for doing business or for allowing the dominated country a measure of political autonomy.”


47. See id. As opposed to buyer-driven commodity chains, producer-driven commodity chains refer to “those in which large, usually transnational, manufacturers play the central roles in coordinating production networks.” The typical example of producer-driven commodity chains is the automobile industry. Profits in the producer commodity chain are gained from “scale, volume and technological advances.”

48. See id.


50. See Miller, supra note 7, at 847.
transplants whose acceptance is motivated by the desire to please foreign states, individuals or entities—whether in acquiescence to their demands, or to take advantage of opportunities and enticements that they offer—many different situations involve this type.” 51 Under the externally-dictated transplant, the degree of the external pressure affects the extent of acceptance in the receiving country. The transplanted law is doomed to be abandoned as soon as the external pressure disappears, unless the law has been internalized by the receiving country. 52 The following section examines how a receiving country (society) reacts to the externally-dictated transplant.

III. THE TRANSPLANT EFFECTS: CHINA AS A CASE STUDY

What are the effects of such transplants on the receiving country (or society)? This section examines two examples of social and environmental standards that are usually mentioned in multinational companies' codes of vendor conduct: SA8000 and ISO 14001. The two standards are representative because of their worldwide applicability and popularity. They produce different outcomes after being transported by multinational companies to China. The China case study also indicates the potential and limitations of legal transplants through private contracting.

A. Socially Responsible Production Standards: SA8000

SA8000 is a set of auditable labor standards established by the Council on Economic Priorities Accreditation Association (CEPAA) in 1997 and now administered by SAI. SA8000 addresses compliance with national law, International Labor Organization Conventions, the UN's Universal Declaration of Human Rights, and the Convention of the Rights of the Child. 53 To measure a company's labor protection performance, SA8000 provides criteria for nine areas including child labor, forced labor, health and safety, freedom of association and rights to collective bargaining, discrimination, discipline, working hours, compensation, and management systems. To be certified under SA8000, a facility must first conduct a preliminary internal assessment of compliance with SA8000 and make any changes to conditions and policies required by the standard. Then an auditing company accredited by the SAI conducts an initial assessment and provides corrective action requests for the applicant facility. After making changes in accordance with the corrective action requests, the facility contacts the auditing company to arrange a full certification audit. If it passes the audit, the facility will be certified. Surveillance audits periodically occur thereafter. The cost of

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51. See id.
52. See id. at 868.
53. See Article II of SA8000 Standard.
obtaining a SA8000 certification can be categorized into two types: the certification fees and the corrective/compliance costs. As to the corrective/compliance costs, the amount can vary from facility to facility depending on factors such as the degree of non-compliance and the number of workers.

As of March 31, 2008, China ranked as the third largest country in terms of the number of SA8000-certified facilities and the second largest country in terms of the number of workers covered under the standard. The growth of SA8000 in China is attributable to the external pressure from foreign buyers. I have discussed elsewhere in great detail the SA8000 development in China so that a short summary may suffice here. Briefly speaking, the Chinese government and suppliers generally resist SA8000. They suspect that the ulterior motive of SA8000 and similar standards is to undercut developing countries' competitiveness by raising their labor costs. Moreover, the chaotic certification market in China makes Chinese suppliers believe that SA8000 is an extortion scheme, paying off auditors in exchange for a responsible production label. Also, they charge that SA8000 and other similar standards ignore the reality that most of the indigenous companies are still in early stages of development and accumulation of capital. During this stage, many companies lack the resources for labor protection. Finally, and most importantly, global buyers refuse to bear the costs of improving labor conditions, which places suppliers in developing countries in a very difficult economic situation.

As Professor Jonathan Miller argues, in an externally-dictated transplant, the receiving party would focus in particular on the costs and benefits of compliance and noncompliance. The development of SA8000 and other similar standards in China in recent years is consistent with this theory. Since global buyers with strong bargaining power condition business on implementation of vendor codes, in order to obtain business, suppliers accept the condition. However, it is very difficult for suppliers to faithfully implement the codes because their implementation (in particular wages, work hours, insurance, and

54. See Social Accountability Accreditation Services, Certified Facilities List, available at http://www.saasaccreditation.org/certfacilitieslist.htm#summary (last visited July 11, 2008). As of Mar. 31, 2008, the number of certified facilities by country: Italy (795), India (267), China (214), Brazil (94), Pakistan (52), Vietnam (38), Thailand (24), Spain (20), Portugal (11), Taiwan (11), Greece (9), Indonesia (9), and the Philippines (9). Under SA8000, 872,052 workers were covered (200,215 workers in India and 186,761 in China).


56. For a detailed discussion, see Li-Wen Lin, Corporate Social Accountability Standards in the Global Supply Chain: Resistance, Reconsideration and Resolution in China, 15 CARDOZO J. INT'L & COMP. L. 321 (2007).

57. See Miller, supra note 7, at 876.
pension) incurs substantial costs and because, as many Chinese suppliers claim, they cannot demand increased prices from foreign buyers to reflect the costs. Therefore, it is no surprise that many suppliers falsify labor protection records to get business. The suppliers calculate the compliance level based on a cost-benefit analysis. In response to the compliance problem, global buyers usually intensify auditing, making code implementation like a cat and mouse game.

Moreover, as Professor Miller notes, when a transplant is driven by foreign pressure, it may produce an unintended or counterproductive response from the receiving country, and such a response may depend on political and cultural factors prevailing there. The development of SA8000 and similar standards in China offers a concrete example. Some Chinese suppliers have taken unanticipated measures to respond to the legal transplant by global buyers. Since Chinese suppliers individually cannot reject the import of vendor codes by their foreign buyers, some suppliers in the textile and apparel industries, where foreign vendor codes are common, have tried to gain leverage against foreign vendor codes by forming associations and developing their own standards. A prominent example is CSC9000T, which was developed by the China National and Textile and Apparel Council and other representatives of Chinese corporations. CSC9000T is a social management system. It sets forth objectives in the areas of management systems, employment contracts, child workers, forced or compulsory labor, working hours, wages and welfare, trade unions and collective bargaining, discrimination, harassment and abuse, and occupational health and safety.

At first glance, CSC9000T looks very similar to SA8000. Yet, CSC9000T is not a set of standards designed for certification. It builds on a model in which third-party evaluation organizations evaluate the suppliers' social performance and give advice on how to improve it. Therefore, CSC9000T takes a much softer approach than SA8000. The standards set forth in CSC9000T are long-term goals.

58. See Lin, supra note 56; see also Poland Li, CSR in the Supply China, CSR ASIA WEEKLY, Vol. 24, Week 28, July 2008, at 12 (reporting interviews with suppliers in China and finding that it seems true that no suppliers really can fully comply with the standards because suppliers cannot pass the costs to global buyers). CSR Asia is the leading NGO with a focus of promoting corporate social responsibility in China.

59. See Lin, supra note 56; see also Wal-Mart 2005 Report on Ethical Sourcing (finding the frequent use of "double books" to hide the numbers of hours worked or wages/benefits paid by suppliers); Gap, Inc. 2004 Social Responsibility Report (finding cases of record falsification in 2003 and 2004); Nike FY04 Corporate Social Responsibility Report (finding record falsification is an obstacle in China).


61. See Miller, supra note 7.

but do not require immediate compliance. The Chinese suppliers further soften the stiffness of social performance by maintaining control over the whole evaluation process. This process is controlled by the Responsible Supply Chain Association (RSCA) whose members are essentially the very companies that are subject to the evaluation process. Given the softness of CSC9000T, western buyers and NGOs may suspect that CSC9000T is merely a contrivance to forge a responsible production label for Chinese suppliers rather than a genuine device to protect labor rights. While it may be too early to tell the true motive behind CSC9000T, based on the 2006 CSC9000T Annual Report, it seems that CSC9000T may herald a Chinese way of implementing socially responsible standards.63 The Annual Report discloses the identity of ten companies that participated in the experimental program under CSC9000T. It also discloses the preliminary evaluation results, showing serious and prevalent violations of minimum wages, working hours, and health protection. Such a disclosure may weaken the suspicion of deception. It also addresses in particular the harmonious and cooperative interaction between the evaluated companies and the evaluators during the evaluation process, the importance of training and technical support, and the flexibility of correcting problems with different urgency levels. Although CSC9000T uses so-called "third party evaluation organizations," it does not stress the independent or adversarial dimension that is typically associated with a third-party auditor. Rather, according to the Report, it is the "cooperative and harmonious" relationship between the CSC9000T evaluators and the evaluated companies that inspires corporate commitment to labor rights improvement.64 The emphasis on such a cooperative and harmonious relationship may have its root in the Chinese cultural preference for non-adversarial mechanisms such as mediation and conciliatory negotiation to resolve disputes,65 but it also strongly reflects the cross-country finding that capacity-building assistance to suppliers in developing countries is an important complement to adversarial monitoring for effective implementation of socially responsible production.66 In short, faced with SA8000 and similar


64. See id.

65. See Carlos de Vera, Arbitrating Harmony: 'Med-Arb' and the Confluence of Culture and Rule of Law in the Resolution of International Commercial Disputes in China, 18 COLUM. J. ASIAN L. 149 (2004) (arguing the Chinese arbitration system that intermingles the conflicting roles of arbitration and mediation, which undermines the impartiality of arbitrators from a western view, has its root in the Chinese cultural preference for harmony).

66. See Richard Locke et al., Does Monitoring Improve Labor Standards?: Lessons from Nike (MIT Sloan School of Management Working Paper No. 4612-06, July 2006) (arguing that after surveying over 800 of Nike's suppliers in fifty-one countries, moni-
standards imposed by global buyers, Chinese suppliers are trying to find their own way to strike a balance between satisfactory working conditions and cruel business reality.

B. Environmentally Responsible Production Standards: ISO 14001

ISO 14001 is a set of environmental management standards developed by the ISO. ISO 14001 was first published in 1996 and revised in 2004. ISO 14001 is a management tool for an organization to control the impact of its activities, products, or services on the natural environment. The environmental management system under ISO 14001 is process-focused rather than substance-oriented. As a result, an organization in compliance with ISO 14001 does not itself guarantee environmentally responsible performance. Still, ISO 14001 accompanied by auditing mechanisms provides an important tool for a firm that wants to demonstrate its commitment to environmental protection.

As of December 2006, China ranked as the second largest country in the number of ISO 14001 certificates. Empirical studies have shown that multinational companies' procurement policies presses Chinese suppliers to be certified under ISO 14001. Foreign pressure, however, is not a sufficient account of the rapid growth of ISO 14001 in China because implementation of SA8000 is also encouraged by foreign buyers but has so far received limited acceptance.

In contrast to the SA8000's difficult acclimatization to Chinese society, ISO 14001 enjoys relatively easy acceptance in China. These

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67. See the website of ISO, at http://www.iso.org/.

68. The top ten countries are as follows: Japan (22,825), China (18,842), Spain (11,125), Italy (9825), United Kingdom (6070), South Korea (5893), United States (5585), Germany (5415), Sweden (4411), and France (3047). See ISO, The ISO Survey 2006, available at http://www.iso.org/iso/survey2006.pdf (last visited Aug. 21, 2008).


different fates can be attributed to four factors: the content of the standard, the standard setting process, the goal of the standard, and the local policy in China.

As to the content, SA8000 is a set of substantive standards, while ISO 14001 is a set of management process standards. Compared with the rigidity of substantive standards, the process-oriented feature offers flexibility for different business entities at different development stages in different regulatory environments.71 This flexibility allows them to take local circumstances into account and thus reduces irritation. But it may also indicate that suppliers have more authorized discretion in maneuvering environmental performance without incurring the charge of "falsification."

As to the standard setting process, ISO 14001 is produced through international negotiation. ISO is composed of national standardization institutes from 157 countries, comprising of one member per country.72 Each member body is represented by the most representative standardization institution in its country. The representative institution may be in the public or private sector. The representative institution of China has always been part of the government.73 China has participated in the ISO 14001 standard-setting process since the very beginning.74 This participation may tone down the sharp foreign image of the standard. In contrast, the socially responsible production standards are currently developed either by western organizations or companies without substantial input from developing countries in which the standards are actually implemented. This also implies the great potential of ISO 26000, a new set of socially responsible production standards that will be completed in

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71. According to the explanation provided by ISO, ISO 14001 is known as "generic management system standards." "Generic" means the standard can be applied to any organization, large or small, whatever its product, in any sector of activities, whether it is a business enterprise, a public administration, or a government department. See ISO, ISO 9000 and ISO 14000 – in brief, available at http://www.iso.org/iso/en/iso9000-14000/understand/inbrief.html.


73. The People's Republic of China became a member of ISO in 1978 with China Association for Standardization (CAS) as the representative institution. CAS was replaced by China National Standardization Institute (CNSI) in 1985. CNSI was replaced by the General Administration of Quality Supervision, Inspection and Quarantine of the People's Republic of China in 1989. Because the governmental organization reform in China, now Standardization Administration of China (SAC) established by the State Council of China in 2001, is the representative institution for China. See http://www.sac.gov.cn/english/cnorg/index2.asp (last visited Aug. 25, 2006).

74. The delegation of the State Environmental Protection Administration of China participated in the meetings concerning environmental protection (ISO/IEC SAGE) held by ISO in 1991 and 1992. China also has participated in the meetings later held by ISO/TC207 since 1993.
2010 by the ISO.75 The participants in the ISO 26000 standard-setting process include not only developed but also many developing countries such as China. However, ISO 26000 will only be a set of guidelines rather than certifiable standards. The guideline model limits the potential of ISO 26000, but it also reflects the actual disagreement on labor standards among countries that bring their local concerns into the negotiation.

With regard to its goal, ISO 14001 is designed with a view to facilitate trade and remove non-trade barriers.76 The WTO has affirmed the link between trade and environment and recognized that each member country has the right to take measures for environmental protection so long as they are not arbitrary and discriminatory.77 Therefore, when countries have conditioned import on diverse environmental standards, which may create compliance difficulties for international traders, ISO 14001 can be seen as a mechanism to coordinate conflicting environmental requirements and international trade. However, SA8000 does not share the same background. The trade and labor protection linkage has been hotly debated in recent years and decisively thrown out of the Doha negotiation agenda.78

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76. ISO/TC207, the technical committee for ISO 14000 of the ISO, declares that “ISO/TC 207's vision is the worldwide acceptance and use of the ISO 14000 series of standards which will provide an effective means to improve the environmental performance of organizations and their products, facilitate world trade and ultimately contribute to sustainable development” and “TC 207 has tried to create a positive mechanism for improving trade, while encouraging improvements in environmental performance. Its challenge now is to help ensure that the standards are used as intended, and not as a barrier to trade.” See http://www.tc207.org/about207.asp#background and http://www.tc207.org/faq.asp?Question=15 (last visited May 4, 2007). ISO has also reached an agreement with WTO with the common goal of promoting a free and fair global trading system, in which standardizing bodies subject to the agreement are required to develop standards based on the Code of Good Practice for the Preparation in the WTO's Agreement on Technical Barriers to Trade (TBT) and follow certain notice procedures. See ISO, ISO and Trade, at http://www.iso.org/iso/en/aboutiso/introduction/index.html#eight (last visited May 4, 2007).
77. At the end of Uruguay Round in 1994, trade ministers from participating countries created Trade and Environmental Committee, bringing the environmental and sustainable issues into the mainstream of the WTO. The Doha negotiation round also has included environmental issues such as the coordination between the WTO and multilateral environmental agreements. See also the prominent “Shrimp-Turtle” case, in which the Appellate Body affirmed countries have the right to take trade actions to protect environments so long as certain requirements, such as non-discrimination, are met. See Appellate Body Report, United States—Import Prohibition of Certain Shrimp and Shrimp Products, WT/DS58/AB/R (Oct. 12, 1998).
78. For the literature on trade-labor linkage, see, e.g., Clyde Summers, The Battle in Seattle: Free Trade, Labor Standards, and Societal Values, 22 U. PA. J. INT'L ECON. L. 61, 87 (2001) (arguing that “[d]eveloping countries can retain their legitimate comparative advantages while recognizing at least minimum fundamental values”); Michael J. Trebilcock & Robert Howse, Trade Policy & Labor Standards, 14 MINN. J. GLOBAL TRADE 261, 279 (2005) (arguing that trade sanction should apply to violation of core labor standards and some generally accepted human rights, e.g., genocide, torture, and detention without trial); Daniel S. Ehrenberg, The Labor Link: Applying the
This means that trade-labor barriers imposed by governments are hard to defend under the scrutiny of international trade law. SA8000 itself seems to be a trade barrier when adopted by multinational companies in supply chains.

The governmental policy in China also gives a profound account of the different acceptability of ISO 14001 on the one hand and SA8000 on the other by Chinese suppliers. ISO 14001 has been transformed into its national legal system and into concrete measures. The State Environmental Protection Administration of China (SEPA) started to implement ISO 14001 in several cities in 1996. In 1997, the SEPA instituted the China Steering Committee for Environmental Management System Certification (CSCEC) to formally construct the implementation platform for ISO 14001 in China. The responsibilities of CSCEC include administering consultation, certification, and training. The SEPA also had approved thirty-two National Model Areas for ISO 14001 by the end of January 2007. Furthermore, the SEPA has formalized the establishment procedure of National Model Areas for ISO 14001 to systematically promote ISO 14001. The Chinese government's support is particularly helpful to create a policy climate that is friendly to ISO 14001. In such a climate, Chinese suppliers do not have a strong position to argue that ISO 14001 is an unreasonable burden imposed by powerful global buyers. In fact, the promotion of ISO 14001 is a domestic state policy in China. Even if Chinese suppliers are not really willing to accept ISO 14001, their complaint would be suppressed in such a political climate.

C. Evaluation

It is difficult to claim that vendor codes in global supply chains are successful legal transplants in China if success is measured by the gap between the law in contracts and the law in implementation. But the impact of a legal transplant may be an issue much broader

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In the 1996 Singapore Ministerial Declaration, the WTO rejected the use of labor standards for protectionist purposes and believed the competent organization for labor issues should be ILO. The 2001 Doha Ministerial Conference reaffirmed the Singapore declaration on labor without any specific discussion. See WTO, Labor Standards: Consensus, Coherence and Controversy, at http://www.wto.org/english/tratop_e/labsud_e/whatis_e/tif_e/bey5_e.htm (last visited May 4, 2007).

79. See the official documents concerning the establishment of CSCEC (State Council [1997] No. 27; Environment [1997] No. 379) issued by the State Council and the State Environmental Protection Administration of China (on file with author).

80. See the official directory of the model areas issued by SEPA (or ZHB, in Chinese), at http://www.zhb.gov.cn/tech/ISO14000/rkjx/200405/t20040531_90316.htm (last visited May 4, 2007).

than the question concerning the implementation/compliance degree of the transplanted law itself. In fact, the proliferation of vendor codes in global supply chains creates an opportunity for Chinese policymakers to reconsider the role of corporations in economic development. In other words, legal transplants via private contracting help some changes in government policy, which in turn affects the acceptability of the privately transplanted law.

For years, Chinese scholars and policymakers have debated the reasonableness of vendor codes in global supply chains and the rationality of CSR, the core idea underlying the vendor codes. The Chinese literature on CSR topics has grown noticeably in the recent few years, and it generally assumes vendor codes in global supply chain trigger the CSR discussion in China. The idea of CSR imported in the vendor codes helps to create a focus of the discussion. The debate has very recently settled on accepting the idea of CSR and of responsible production standards, though with some qualifications as shown below. The discussion has also resulted in some important legal reforms. The leading example can be seen in the recently revised Chinese Company Law, which took effect on January 1, 2006. The law clearly requires Chinese companies to "undertake social responsibility" in the course of business. It thus provides a legal foundation for vendor codes in China.

Also, following the recognition of CSR in the 2006 Company Law, a number of state-driven CSR initiatives have recently emerged in China. An important example is the Guide Opinion on the Social Responsibility Implementation by the Central-Government-Controlled State-Owned Enterprises ("Guide Opinion") released by the State-Owned Assets Supervision and Administration of the State Council (SASAC). The SASAC supervises 150 Chinese state-owned companies, all of which are large and important. According to the SASAC's statement, the organization recognizes that there is a proliferation of CSR initiatives at the global level, including the UN Global Compact, ISO 26000, and multinational companies' codes of conduct. But in the SASAC's view, the contents and measures of CSR in China were

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not clear, so the SASAC conducted a two-year study and produced the Guide Opinion for the Chinese state-owned enterprises to follow.\(^\text{86}\) The SASAC also intends to encourage the Chinese state-owned enterprises to set CSR examples for all Chinese companies to follow suit.\(^\text{87}\) It declared that the Guide Opinion is consistent with international standards but also compatible with the national and organizational reality in China.\(^\text{88}\) The Guide Opinion lays out the basic contents of CSR in China requiring the companies to fulfill a long list of requirements: comply with the law; improve product quality; reduce emission and waste; provide safe, healthy, and clean working conditions and living environments for workers, and; protect workers’ legal rights (such as signing and implementing employment contracts, launching pay-raise mechanisms, paying the full amount of social insurance in a timely manner, strengthening employee training, and avoiding discrimination, etc.). It also suggests that the companies establish CSR management and reporting systems. Partly because of SASAC’s promotion, some important Chinese state-owned enterprises have already engaged in CSR reporting.\(^\text{89}\) All of these measures are consistent with vendor codes in global supply chains. This is not to say that China fully accepts CSR as generally understood in western countries. The SASAC explicitly refers to the UN Global Compact, which requires companies to “support and respect the protection of internationally proclaimed human rights; and make sure they are not complicit in human rights abuses,” while the Guide Opinion implicitly excludes human rights issues from the Chinese CSR agenda. The exclusion of human rights may be one of the SASAC’s so-called “CSR with Chinese characteristics.” In short, the Chinese government accepts the labor and environmental aspects of CSR and vendor codes, but it rejects the human rights aspect. In a political climate where human rights issues are strictly controlled by the government, it is no surprise to find that no Chinese private CSR initiatives (e.g., CSC 9000T and the Social Responsibility Guide that was launched by the Chinese Industrial Companies and Industrial Associations) cross the red line; none of them include human rights issues.\(^\text{90}\)

\(^{86}\) See id.

\(^{87}\) See id.

\(^{88}\) See id.

\(^{89}\) The companies include China National Petroleum Corporation, State Grid, China Mobile, China Ocean Shipping Group (COSCO), China Huaneng, China Datang, Sinochem Corporation, Sinopec, SinoSteel, Aluminum Corporation of China, Bao Steel, CNOOC, etc.

China has multiple motives for adopting the Chinese version of CSR. As some Chinese commentators advocate, adopting specifically Chinese CSR standards can prevent SA8000 or other similar western standards from becoming universal. In other words, the construction of Chinese CSR standards can be a defense against the imposition of western norms.

The reason behind adopting CSR standards in China is not simply that global buyers require them but also, and probably more importantly, the Chinese government's domestic economic and political interests in adopting the modified version of CSR. The Chinese government has recognized that the labor-exploitation and environment-pollution production model has reached a bottleneck in economic development so that a redirection of macroeconomic development strategy is necessary. The Chinese government has recently employed an array of tax measures and export regulations to force companies to move up the value chain, from low-skilled and labor-intensive to high-skilled and technology-intensive work. For example, it has taken tough measures on labor-intensive and low-technology manufacturers in export processing zones, including export restrictions on nearly 2000 kinds of labor-intensive/low-technology products, substantial increases in tax rates, and elimination of other regulatory exemptions. These measures have caused a large wave of shutdowns or relocations of companies in the economically developed areas (e.g., the Pearl River Delta), according to scores of major Chinese news reports. CSR and vendor codes are consistent with the new economic development policy, helping to purge companies that cannot meet good social and environmental performance.

Moreover, in the past few years, domestic social and environmental problems have become serious and even resulted in social unrest, which may eventually threaten the Chinese Communist Party's ruling authority. In October 2006, the Sixth General Meeting of the Sixteenth Central Commission of the Chinese Communist Party made an important declaration that "building a harmonious society"
is a long-term goal of Chinese socialism. According to the declaration, there are many existing problems that can cause conflicts and damage social harmony, mainly including inequality in regional development, population pressure and environmental pollution, unemployment, income inequality, and low accessibility and low quality of health care and social security. The declaration also makes clear that solving these problems is currently the principal agenda of the Chinese Communist Party. CSR and vendor codes in fact address many of these problems. In this regard, the Chinese government's adoption of CSR and vendor codes is a measure to implement this newly-minted political ideology ("social harmony") in China.

In summary, vendor codes in global supply chains have caused two transplant results in China. First, they have made some Chinese companies improve their social and environmental performance, although many Chinese suppliers are still struggling to honestly implement the codes. The gap between the law in contracts and the law in practice seems still large. Second, the code proliferation in global supply chains has successfully triggered policy discussion in China, facilitating some changes in government policy. In other words, the bottom-up legal transplant has brought about top-down CSR measures in China that are an important factor influencing the acceptability of the transplanted law through private contracting.

IV. THEORETICAL DISCUSSION AND FUTURE RESEARCH

The existing legal transplant literature generally focuses on relocation of law across jurisdictions through governmental channels (e.g., legislatures or courts). This Article has directed attention to a generally ignored phenomenon: law can also be transplanted through contracting between private parties. Arbitration clauses and codes of vendor conduct in global commercial contracts are great examples. The transplanted law in private contracting may include not only private law but also, more importantly, public law (e.g., human rights, labor, and environmental law).

Given that there are alternative ways of legal transplantation, future research might focus on the differences between legal transplants via governmental and private channels and on the comparative advantages of each channel in a given context. Let us here consider some possible advantages of legal transplants through private contracting.

First, sometimes it may be easier to transplant through private contracting than through governmental legislation because it may avoid political or bureaucratic obstacles. It may be easier for two business parties to reach an agreement than for a large number of political representatives to reach a consensus. Second, legal transplants through private contracting can be a potential bottom-up
approach of legal reform. For example, since some types of law, such as human rights, are politically-sensitive, some governments may not be willing to transplant because it may threaten their political power. But when a transplant is attached to a lucrative commercial transaction, private actors may be well-motivated to transplant the law despite its political implications. For private parties, business interests in everyday life are usually far more important than political ideologies enshrined in the political forum. Third, legal transplants through private contracting may be more likely to take real effect because private actors in a real business world may know better what transplants fit their needs and to what extent they would be effective. When a party to the contract fails to implement the transplanted law, the other party who is negatively affected by the implementation gap may have strong incentives to quickly correct the problem through renegotiation or other remedial measures. For example, when Gap and Nike were publicly criticized for their suppliers' labor exploitation practices in developing countries, these companies quickly intensified monitoring their suppliers to ensure compliance with the transplanted law and therefore to protect their corporate images.

But the possible advantages of legal transplants through private contracting also imply important risks. For example, although legal transplants through private contracting may avoid inefficient political discussions, they also raise accountability concerns. When a legal transplant is through governmental legislation, different interested parties have a chance in the legislative process to air their views, at least theoretically and in democratic countries. The legislative process may serve as a filter to control the suitability of the transplanted law. The legislative body is held accountable for the result of the transplant. When a legal transplant occurs through the judiciary, the courts assume responsibility for the result. The quality and suitability of the transplanted law may be assured by the appeal system. But who is held accountable for the transplant effect when it is the result of private contracting? Does the private contracting process offer comparable deliberation and quality control? This is a particularly acute issue when the transplanted law is regulatory in nature and has an impact on the interests of third parties who probably do not have a chance to air their opinions in the contracting process. In the example of vendor codes in global supply chains, the greatest beneficiaries of the legal transplants are the workers at the factory and the local communities around the factory. But worker and local community participation in the contracting process is usually none or at best minimal. Multinational companies are pressured by their major

93. The lack of participation by workers and local communities in developing countries has been criticized by NGOs. Therefore, more and more multinational companies now begin to take a so-called "stakeholder dialogues" approach to bring the
markets, mainly in developed countries, to maintain a reputation of responsibility, but they are also pushed by the same markets to offer competitive prices. Since suppliers with relatively weak bargaining power have a narrow profit margin, some of them will falsify labor and environmental records to protect their profits. This, in turn, will undercut the function of the transplanted law, i.e., the protection of workers and environments in the production process. In other words, the legal transplant through private contracting is extremely vulnerable to the economic interests of the contracting parties. When these economic interests do not support the transplanted law, the transplant may be quickly eliminated from the contract, even though the legal transplant can bring crucial benefits to non-contracting parties (e.g., workers). Although there is a possibility that non-contracting parties who have interests in the contract may make claims as “intended third-party beneficiaries” to protect their interests, the Wal-Mart and GUESS? cases suggest that non-contracting parties stand little chance to succeed in this regard. It is not uncommon that supply contracts even include a “no third-party beneficiaries” clause to prevent non-contracting parties from making such a claim to begin with. All this raises serious questions about the reliability of a legal transplant attached to a private commercial contract as an alternative to public legal reform.

Also, legal transplants through private contracting may be much less transparent than transplants through legislative or judicial processes. Contracts between private entities are usually confidential. In the vendor code example, the details of the transplanted law (i.e., the implementation details of vendor codes) are usually confidential and not released to the public. In this fashion, commercial/trade secrets may be a barrier to transparency.

It is also important to consider the role of lawyers in the contracting process. The major, if not the only, legal experts in the process are lawyers representing the contracting parties. Do these stakeholders in the discussion process. But the process is still mainly controlled by multinational companies and western NGOs.

94. In Aug. 1996, a group of workers filed a law suit against Guess? for violations of minimum wages and work hours. One of the workers’ claims was based on the theory of intended third-party beneficiaries. But Guess? urged workers in the contracting shops to waive their rights to participate in the lawsuit. See ESBENSHADE, supra note 34, at 2. On Sept. 3, 2005, a group of Bangladeshi, Chinese, Indonesian, Nicaraguan, and Swazilander workers also launched a suit against Wal-Mart for alleged violations of Wal-Mart’s vendor code, based on the theory of intended third-party beneficiaries. But the court dismissed the plaintiff’s claim based on the reasons that third-party beneficiaries can only enforce a contract against the promisor, which is the suppliers, not Wal-Mart in this case, and Wal-Mart has the right—not the obligation—to inspect the factories. Moreover, when making claims across borders, the plaintiff in developing countries may also confront the problems such as forum non conveniens and failure of showing exhaustion of remedies in the plaintiff’s home country.
lawyers consider the local circumstances on a case-by-case basis, or do they just copy and paste standard contracts? To find an answer requires further research. But at least in the case of vendor codes, the latter alternative seems to be more likely.

Besides the accountability and quality concerns, legal transplants through private contracting also raise efficiency concerns from a legal reform perspective. The transplanted law in private contracting usually applies to a limited number of parties—Nike's code of conduct only applies to Nike's suppliers. To effectuate a legal reform in a jurisdiction (e.g., setting up safety standards in workplaces in China) would require numerous negotiations and contracts among a large number of private parties. In addition, a private legal transplant initiator is unlikely to reach all entities that should be subject to the transplanted law; it is impossible, and does not make any sense, for Nike to contract with all manufacturers in China. But the coexistence of many private initiators to transplant a certain kind of law through contracting involves the risk of inconsistency, unless there is coordination between them. For example, although many multinational companies have adopted vendor codes referring to the same international law, their codes still vary greatly in detail. Legal transplants through private contracting therefore may create multiple, and conflicting, legal orders concerning the same issue in the same jurisdiction. While this is not necessarily bad, as multiple orders may reflect the need for flexibility—different companies may just need different standards—it is a reason for concern and caution. It shows that legal transplants through private contracting may not be an efficient way to carry out a large-scale legal reform.

Still, legal transplants through private contracting may play an experimental role in the legal reform process. A legal transplant through private contracting can test on a small scale whether the transplanted law is compatible with the institutional environments of a receiving country and allow quick modifications through renegotiation. If the experimentation succeeds, a legal transplant through private contracting may be upgraded to a legal transplant through legislation, and based on the information gained by the experiment, it may be easier for the government in the receiving country to choose a transplant that is compatible with the local environment.