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## **From transnational soft law to national hard law? – regulating supply chains**

### **Abstract**

The paper takes ‘subcontracting’ as a basis for a legal case study and aims to explore how the basically voluntarily developed, CSR-inspired, transnational (self)regulatory ideas of chain-responsibility might percolate into national hard laws. The core idea of subcontracting-related regulatory experimentations is to make actors other than the direct employer co-responsible or liable for ensuring some (or all) labour and social rights of workers employed in the supply chain. This ‘co-responsibility’ can be advanced both by ways of soft law and hard law. The paper offers an overview of these emerging regulatory mechanisms and tries to highlight their implications and ‘spill over’ effects in terms of labour law.

Both on the transnational and national level various non-legal and legal approaches are applied and proposed to address the impact of subcontracting on labour rights. This paper, at first, presents a general descriptive analysis of these regulatory ideas and responses, then it describes some related transnational soft law measures, some regulatory proposals / concepts and some national hard law mechanisms. Finally, the paper reflects on some possible synergies between the soft and hard law approaches in this field.

### **Keywords**

CSR (Corporate Social Responsibility), subcontracting, supply chain, hard law – soft law, labour law, employers’ liability, due diligence.

### **1. Subcontracting and its effects on working conditions**

Subcontracting has shown a boom in the last decades. The emerging idea of chain-responsibility reflects the fact that businesses around the world have witnessed significant structural changes in recent decades. Owing to international business transactions and global production networks, the boundaries of enterprises blur. Today’s multinationals lack vertical integration, they are rather networked in complex production and labour webs of subcontracting chains. The globalization of supply chain management is characterised by additional challenges, such as the differing

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levels of labour standards, the fragmentation and decentralization of multi-layered corporate structures that all add to the complexity of the relationship with suppliers. Business enterprises are increasingly disaggregated into smaller independent parts and services and production are often shifted to these independent third-party suppliers.<sup>1</sup> The growing use of subcontracting led to concerns about the possible deterioration and under-enforcement of labour rights<sup>2</sup>, especially at the bottom of the supply chains.<sup>3</sup> Decent work is often unachievable for those who are at the bottom of supply chains. This can be explained by the downgrading effect of subcontracting on working conditions<sup>4</sup> and by the enforcement difficulties created by complex corporate structures.<sup>5</sup> Furthermore, subcontracting can have a detrimental effect on workers' organization and channels of collective voice. On the other hand, subcontracting seems to be a standard business technique as it is generally accepted as a value-enhancing method in modern economic activity.

In general, subcontracting and outsourcing have two main motivations for end-users: efficiency-enhancement<sup>6</sup> and limitations on legal liability (avoidance of the employer status, decreasing direct responsibility, transference of business risks onto others).<sup>7</sup> In other words: maximising flexibility while minimising costs. Needless to say, these are rational business logics.<sup>8</sup> While the trends in subcontracting are – at least partly – about externalizing responsibility, various new legal mechanisms (hard and soft) are trying to rebuild responsibility, at least to some extent. Both on the transnational and national level various non-legal and legal approaches are taken and proposed to address the impact of subcontracting on labour rights (in this paper we understand and scrutinize subcontracting or chain-liability laws in the broadest possible sense). This article at first offers a general descriptive analysis of these regulatory ideas and responses, then it describes some related transnational soft law measures, some regulatory proposals / concepts and some national hard law mechanisms. Finally, the paper reflects on some possible synergies between the soft and hard law approaches in this field.

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<sup>1</sup> Glynn, Timothy P., 'Taking the Employer Out of Employment Law? Accountability for Wage and Hour Violations in an Age of Enterprise Disaggregation' (2011) *Employee Rights and Employment Policy Journal*, Vol. 5, Issue 1, 101-135.

<sup>2</sup> Cf. Davidov, Guy, 'The Enforcement Crisis in Labour Law and the Fallacy of Voluntarist Solutions' (2010) *International Journal of Comparative Labour Law and Industrial Relations*, Vol. 26, 61-82; Zahn, Rebecca, 'Crisis in Labour Law', University of Kingston, 11th May 2012: (with N. Busby) 'European Labour Law in Crisis: the Demise of Social Rights?'

<sup>3</sup> See for further details: Hajdú József, 'Protection of workers' rights in subcontracting in Europe', Conference Paper, MTA-PTE Összehasonlító és Európai Foglalkoztatáspolitikai és Munkajogi Kutatócsoport, Constitutive Meeting, Recent Developments in Labour Law, 25-26. October 2012, Pécs, Hungary.

<sup>4</sup> Subcontracting might 'foster race to the bottom in working conditions'. European Parliament, 26 March 2009, (2008/2249(INI)).

<sup>5</sup> De Luca-Tamajo, Rafael & Perulli, Adalberto, 'Labour law (in its individual and collective aspects) and productive decentralization', General Report (2006); International Society of Labour and Social Security Law – XVIII World Congress of Labour and Social Security Law, Paris 5-8 September. Morin, Marie-Laure, 'Labour law and new forms of corporate organization' (2005) *International Labour Review* Vol. 144. No.1.

<sup>6</sup> See for basics in law and economics: Coase, Ronald H., 'The Nature of the Firm' (1937).

<sup>7</sup> Glynn (n 1) 103.

<sup>8</sup> Cf. James, Phil & Johnstone, Richard & Quinlan, Michael & Walters, David, 'Regulating Supply Chains to Improve Health and Safety' (2007) *Industrial Law Journal*, Vol. 36, No. 2.

Subcontracting can create subordination (a specific form of ‘controlled autonomy’<sup>9</sup>), as the economic power of clients / principal contractors can excessively dominate the whole value chain.<sup>10</sup> Thus, again, subordination calls for some kind of legal protection and new enforcement strategies. Civil society organisations (NGOs, consumers’ organisations etc.) and modern business dynamics (such as the idea of CSR) put increasing pressure on transnational enterprises (TNCs) to take responsibility for their supply chain (and for the workers employed also ‘deep down’ in the supply chains). This pressure also has an indirect effect on regulators, as the idea of some kind of chain-responsibility becomes more and more generally accepted.

Traditionally, the end-user (and / or the principal contractor) has no direct legal liability for the working conditions of the employees of its subcontractor, since labour law normally imposes duties only on employers. Notwithstanding, there is an emerging trend towards an innovative legal approach, where imposing some duties on clients and principal contractors is becoming a reality. This idea reflects the true situation, whereas in subcontracting networks the real economic power is not always attached to the ‘de iure’ employers, but to the main contractor (‘de facto’ employer). It is hard to neglect that it is rather difficult to accept these ground-breaking legal concepts, as they extend the employers’ obligation beyond our general, classical perception of the employment relationship. However, without such measures, labour can remain a simple ‘commodified input’ in subcontracting networks.<sup>11</sup>

## **2. Basic regulatory dilemmas and responses**

It is very difficult to accurately delineate how far does the responsibility of corporations (especially that of multinationals) reach in value chains. It is even more difficult to design effective regulatory – self-regulatory (soft law) and / or legislative (hard law) – techniques to implement this kind of responsibility. The core idea of such emerging regulatory experimentations is to make actors other than the direct employer co-responsible or liable for ensuring labour and social rights of workers employed in the supply chain with regard to, for example, minimum wages, social security contributions, occupational health and safety and / or other working conditions.<sup>12</sup>

The idea of chain-responsibility is not yet so well developed in positive law. However, there are some signs of development. Davidov notes on a general level that when employers turn to use intermediaries (such as subcontractors), courts must ask which relationship presents the real vulnerabilities for workers justifying labour law

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<sup>9</sup> Morin (n 5) 12.

<sup>10</sup> In extreme cases, corporate power can represent a form of economic violence, a ‘new form of blackmail’. ORSE, ‘*A critical look by suppliers of the purchasing policies of big corporations*’, September 2007.

<sup>11</sup> Glynn (n 1) 114.

<sup>12</sup> The idea of chain-responsibility might also be associated with the legal doctrine of ‘enterprise liability’. Under this idea, individual entities (for example, otherwise legally unrelated corporations) can be held jointly liable for some action on the basis of being part of a shared enterprise.

protection.<sup>13</sup> He states that ‘in many cases, notwithstanding the formal legal arrangement, it is the ultimate ‘client’ that will have to bear responsibility’.<sup>14</sup> The core idea of chain-responsibility arrangements must be to ensure that subcontracting does not result in escaping labour law’s grasp, and liability is attached to the ‘hub’ company (the ‘real’ power dominating the supply chain). Such - either soft or hard - mechanisms might extend corporations’ labour law-related liability beyond corporate borders and in some cases, to some extent, beyond national borders as well (because subcontracting chains more and more frequently engage companies from different states). In this latter, transnational, cross-border subcontracting situations the issue becomes even more complicated, self-evidently, ex ante blocking the effectiveness of conventional hard law solutions to a large extent. This is because of supply chains’ extreme partition geographically and culturally.

In general, chain-responsibility mechanisms might be interpreted as the breakthrough of the contractual relationship. In corporate law, according to the principle of separate legal personality, as a main rule, each company’s liability is limited to its own entity (this is the so-called separation principle or the principle of autonomy of each company in the network).<sup>15</sup> However, in a labour law context there can be convincing arguments for exceptions to the separation principle, explained by the inherent asymmetric power-relations. Davidov describes the goal of labour laws to be designed to “intervene in the contractual relationship between employer and employee, and often to redistribute resources from one to the other.”<sup>16</sup> In fact, joint liability laws for subcontracting chains are nothing else than the innovative redistribution of responsibility for risks in supply chains’ complex contractual relationships. As such, the rationale of these laws is in principle very near to the traditional idea of labour laws. Joint liability laws are just expanding and realizing labour laws’ original goals with respect to new global economic realities. There is a clear need for such regulatory innovations and expansion, since ‘old-fashioned’ labour laws ‘devised to apply within the hierarchical and bilateral structure of the employer/employee relationship, and they are ill-fitted to tackle the multilateral structure of network production where market and hierarchical relationships are entangled.’<sup>17</sup> Accordingly, joint liability laws might bridge the inherent regulatory gap between labour laws and workers in network firms and offset the inability of labour laws to capture the reality of work in new organizational settings of complex corporate structures. The ultimate goal is to block the circumvention of employers’

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<sup>13</sup> The concept of joint and several liability also seems to be accepted by the European Court of Justice, at least in principle. Cf. Executive Summary, *Study on the protection of workers’ rights in subcontracting processes in the European Union*, Project DG EMPL/B2-VC/2011/0015, Ghent University & University of Amsterdam.

<sup>14</sup> Davidov, Guy, ‘Re-Matching Labour Law With Their Purpose’ (eds.: Davidov, Guy & Langille, Brian) *The Idea of Labour Law* (Oxford University Press 2011) 189.

<sup>15</sup> Saage-Maaß, Miriam, ‘Labour Conditions in the Global Supply Chain, What Is the Extent and Implications, of German Corporate Responsibility’ (2011) IPA, Friedrich Ebert Stiftung 10.

<sup>16</sup> Davidov, Guy, ‘Articulating labour law’s goals: why and how’ (2012) *European Labour Law Journal*, Vol. 3, No. 2. 137.

<sup>17</sup> Martin, Isabelle & Barré, Philippe, ‘Back to basics: A critical assessment of CSR as work law in network firms’, Conference Paper, Inaugural conference of the Labour Law Research Network, Barcelona, June 13-15, 2013.

responsibility and the abuse of workers' rights in supply chains. Without such measures it is easy for businesses to demand quality and low prices without exerting control and liability for operational conditions, including working conditions.

In the various regulatory ideas usually two *basic types* of liability can be differentiated<sup>18</sup>:

- Joint and several liability (often used interchangeably with enterprise liability and chain liability, albeit incorrectly) generally references liability between immediately contracting parties in one segment of the contracting chain (direct liability).
- Chain liability applies not only in relation to the contracting party, but also to the whole chain, so the aggrieved party can seek redress from any link in the entire chain.

The general *justification* for various national joint liability laws is usually framed around three central arguments:

- Social argument: the most solvent, most powerful, influential, superior party should be held liable in a subcontracting network (i.e.: re-linking power and responsibility);
- Economic argument: there is a need for a level playing field and high level of transparency in subcontracting networks to eliminate market-distortions and unfair competition via wage dumping;
- Public finance-related argument: the revenues of the relevant governmental authorities should be protected (especially in terms of taxes, social security contributions).

The main *counter-arguments* in relation to joint liability schemes are centred around the following concerns: ineffectiveness, expensiveness, their complicated nature, unrealistic enforcement, paralyzing the economy by incalculable risks, making unintended connections between distant economic actors etc.

As we will conclude, successful attempts to influence businesses in promoting decent working conditions throughout their supply chains often engage hybrid and reflexive<sup>19</sup> forms of regulation, in which top-down state regulation is combined with market-based measures and initiatives.

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<sup>18</sup> Amon, Matthew R. 'Liability Regulations in European Subcontracting: Will Joint Liability Be The 21<sup>st</sup> century European Approach?' (2010) *The Journal of International Business & Law* Vol. 9. No 1. 235.

<sup>19</sup> About reflexive law, see: Teubner, Gunther, 'Substantive and reflexive elements in modern law' (1983) *Law & Society Review*, Vol. 17. No. 2.; Teubner, Gunther, 'Corporate Responsibility as a Problem of Company Constitution' (1983) EUI Working Paper No. 51, Badia Fiesolana, San Domenico (FI); Rogowski, Ralf - Wilthagen, Ton (eds.), 'Reflexive Labour Law' (1994) Kluwer Law and Taxation Publishers; Barnard, Catherine - Deakin, Simon - Hobbs, Richard, 'Reflexive law, Corporate Social Responsibility and the Evolution of Labour Standards: The Case of Working Time' (2004) ESRC Centre for Business Research, University of Cambridge Working Paper No. 294, CBR research Programme on Corporate Governance.

### 3. Transnational soft law measures

The so-called phenomenon of “Responsible supply chain management (RSCM)”<sup>20</sup> has become an important element of corporate social responsibility (CSR).<sup>21</sup> Good self-regulatory practices in this area can make a significant contribution to supply chain stability and long-term efficiency. RSCM endorses the voluntarily shared responsibility of all parties involved in the supply chain. RSCM can be defined as organisations using their purchasing power to effect positive change in the production cycle and work in partnership with suppliers in order to achieve this. Besides legislative acts (see later), such mechanisms might be laid down in collective labour agreements, codes of conduct<sup>22</sup>, private contracts, responsible sourcing guidelines or simply in corporate policies and industry partnerships. Codes of conduct are by far the most common tools to implement RSCM practices. In fact, RSCM and ethical sourcing / responsible contracting<sup>23</sup> are largely overlapping issues, they are all about building sustainability (including social) criteria into buying/sourcing practices. These criteria can also be implemented as contractual obligations, but the power of end-users (hub-firms) to really convince their suppliers to respect labour rights is always dependent on actual market-positions, commitment and business strategies.

As for the *techniques* of RSCM, they are manifold, ranging from simple programmatic expectations and informal questioning to more formal measures, including assessment, certification, auditing, inspection, monitoring, reporting and capacity-building. In some rather developed systems, the goal is not simply to evaluate or rank (and to exclude<sup>24</sup>) suppliers according to sustainability troubles that they face, but to work with them in partnership to improve standards and to implement long-term solutions. Rigid, highly formalised systems of procedures might have counter-productive effects, so cooperation and dialogues are of utmost importance.<sup>25</sup> Setting up of precautionary measures and identification and spreading of best practices are also important.

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<sup>20</sup> Opijnen, Marjon van & Oldenziel, Joris, ‘*Responsible Supply Chain Management, Potential success factors and challenges for addressing prevailing human rights and other CSR issues in supply chains of EU-based companies*’ (2011) European Union.

<sup>21</sup> RSCM is also often associated with the concepts of SERP (Socially and environmentally responsible procurement) and SSCM (Sustainable supply chain management). Hoejmosse, Stefan U. & Adrien-Kirby A. J., ‘Socially and environmentally responsible procurement: A literature review and future research agenda of a managerial issue in the 21<sup>st</sup> century’ (2012) *Journal of Purchasing & Supply Management* 18 (2012) 232–242; *Promoting occupational safety and health through the supply chain*, Literature Review, European Agency for Safety and Health at Work (EU-OSHA), 2012, 6.

<sup>22</sup> See for further details Sobczak, André, ‘Codes of Conduct in Subcontracting Networks: A Labour Law Perspective’ (2003) 44, Issue 2-3 *Journal of Business Ethics* 225-234; Compa, Lance & Hinchliffe-Darricarrère, Tashia. ‘Enforcing International Labor Rights through Corporate Codes of Conduct’ (1995) 33 *Columbia Journal of Transnational Law* 663-689.

<sup>23</sup> *Responsible contracting: An approach aimed at improving social and labour practices in the property services sector*, Working Paper No. 282, by Andrew Bibby, International Labour Office, Sectoral Activities Programme. Geneva, ILO, 2011.

<sup>24</sup> This is the so-called ‘cut and run’ method (which is highly debated, since it is rather mechanical and, after all, can create unemployment by the discontinuation of the supplier contract).

<sup>25</sup> ORSE, ‘*A critical look by suppliers of the purchasing policies of big corporations*’, September 2007.

The main *motivation* for RSCM practices is the increasing scrutiny from watchdog organizations, NGOs and stakeholders, and the overall social context, which create reputational concerns for powerful, brand-sensitive TNCs.<sup>26</sup> As for internal drivers, top management support and organizational values (such as CSR) are to be mentioned.

The biggest *challenges* of RSCM are the so-called full value chain approach, namely to implement and to control those principles along the whole tangled web, and to collaborate with a wide range of stakeholders. As a consequence, often there is a gap between corporate intentions and applications on the ground. In general, it is very difficult to calibrate the ‘scope of responsibility’ of companies and to define the boundaries of intervention. Furthermore, there is often a conflict between sourcing priorities (such as prices, delivery requirements) and sustainability goals. As a result, considerable empirical evidence exists to suggest that codes of conduct (and other RSCM practices) are not sufficient to implement supply chain responsibility.<sup>27</sup>

The main *value* of such CSR / RSCM-practices is that they put the whole issue of supply chain responsibility on the agenda and made it socially intolerable for TNCs to totally ignore breaches of labour rights in subcontracting networks. As a result, we can say that these practices have paved the way and set the scene for eventually harder legal interventions by justifying the legitimacy of increased accountability demands. To put it differently: RSCM practices prove that corporate responsibility can go beyond the strict confines of the employment contract.<sup>28</sup>

Another related angle of transnational soft law measures comprises *IFAs* (*international framework agreements*). Such transnational legal frameworks, agreed between individual multinational enterprises and global union federations, are designed to protect labour standards in multinational enterprises and their subcontractors and affiliates across different countries and they usually cover all involved dependent worker and provide social protection irrespective of specific employment conditions. According to a European survey, practically all IFAs explicitly indicate that the norms they contain apply to the whole group (including suppliers and sub-contractors), which is much more than the extension of commitments to the supply chain incorporated in codes of conduct.<sup>29</sup> However, according to some other studies, IFAs do not necessarily cover workers who are not part of a direct employment relation with the given TNC.<sup>30</sup>

It is a *joint feature* of these innovative RSCM-related self-regulatory methods that they find their roots in soft law<sup>31</sup>, mostly in the concept and practice of Corporate

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<sup>26</sup> Glynn notes that reputation can easily cut in the opposite direction: ‘It may be easier (and far cheaper) for a visible firm to maintain its reputation as a ‘good employer’ – i.e. offering generous pay and benefits to its workforce – if it offloads low-skilled/low-wage work onto others.’ Glynn (n 1) 114.

<sup>27</sup> Hoejmoose, Stefan U. & Adrien-Kirby A. J. (n 21) 237.

<sup>28</sup> Morin (n 5) 21.

<sup>29</sup> *Promoting occupational safety and health through the supply chain*, Literature Review, European Agency for Safety and Health at Work (EU-OSHA), 2012, 27.

<sup>30</sup> Martin, Isabelle & Barré, Philippe (n 17) 15.

<sup>31</sup> See for the general description of the role of soft law in labour law: Duplessis, Isabelle, ‘Soft international labour law: The preferred method of regulation in a decentralized society’, In: *Governance, International Law & Corporate Social Responsibility* (2008), International Institute for Labour Studies,

Social Responsibility (CSR). They are well-grounded and proliferated in private, non-governmental soft regulation. These practices are applied under public social pressure rather than as a result of state regulation. However, one of the classical functions of soft law is the so-called 'pre-law' function: soft law measures may have the capacity for 'hardening', since they can be a first step in the process of legislation.<sup>32</sup> Soft law measures can also be a so-called 'testing field' of innovative regulatory concepts and source of inspiration or pattern for regulators. As such, ideas in soft law may pave the path for the adoption of hard laws in the future. This phenomenon can also be labelled as the 'spill over' function of soft law<sup>33</sup> and can represent the dynamic of a given field of law (in our case, the dynamic of labour law as a widely interpreted branch of regulation). However, it must be mentioned that positive hard law is generally lagging behind broad regulatory ideas and dynamics and changes of self-regulatory practices. Furthermore, in these specific regulatory terrains (e.g. supply chain responsibility) extensive legal regulation could significantly undermine respective competitive market dynamics (thus, hard regulation is not always and not in all aspects necessarily needed).

#### 4. Regulatory proposals and ideas in the crossroads of soft law and hard law

On the international level, the corporate accountability model seeks to improve the chances of victims of various labour and human rights abuses to use remedies against corporations. In this respect, most importantly, John Ruggie, United Nations (UN) Special Representative on *Business and Human Rights*, highlighted the state's duty to protect, the corporate responsibility to respect and access of victims to remedies as the core pillars of his framework.<sup>34</sup> In this regard, supply chain responsibility and 'due diligence' processes in all operations (including human-rights risk-analysis) must be essential mechanisms. Due diligence and the concept of duty of care are promising areas for legal development, as they can give rise to further obligations.<sup>35</sup>

Similarly, the *European Parliament* adopted a resolution in 2009 on the social responsibility of subcontracting undertakings in production chains.<sup>36</sup> It called on public authorities and all stakeholders to do their utmost to increase the level of awareness among workers of their rights under the various instruments (such as labour law, collective agreements, codes of conduct) that regulate their employment relationship and working conditions in the undertakings for which they work and the contractual relationships in subcontracting chains. The Resolution also warned national public authorities to adopt or further develop legal provisions which exclude

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Research Series 116., ILO; Blanpain, Roger and Colucci, Michele, *The Globalization of Labour Standards, The Soft Law Track* (2004) Kluwer Law International.

<sup>32</sup> Cf. SENDEN, L., *Soft Law in European Community Law* (2004) Oxford: Hart Publishing.

<sup>33</sup> Cf. Alhambra, M. Antonio Garcia-Mun˜oz & Ter Haar, Beryl & Kun, Attila, 'Soft on the Inside, Hard on the Outside: An Analysis of the Legal Nature of New Forms of International Labour Law' (2011) *The International Journal of Comparative Labour Law and Industrial Relations* 27, No. 4. 337–363.

<sup>34</sup> "Guiding Principles on Business and Human Rights: Implementing the United Nations 'Protect, Respect and Remedy' Framework", UN, 21 March 2011. 13.

<sup>35</sup> Saage-Maaß, Miriam (n 15) 17.

<sup>36</sup> 26 March 2009, (2008/2249(INI)).

undertakings from public procurement, where they are found to have infringed labour law, collective agreements or codes of conduct. Most importantly, the Resolution expressed the need to establish a clear-cut Community legal instrument introducing joint and several liability at Community level. The envisaged Community instrument on chain liability would be a way of increasing transparency in subcontracting processes and of securing better enforcement of Community and national law. The theory underpinning this call for joint and several liability laws is that if the upper tier company (principal contractor) can be held liable for the malfeasance of its subcontractors at any tier, the upper tier companies will have a great incentive to personally guarantee that all subcontractors assume their corporate responsibility in respect of employee's rights.<sup>37</sup> As such, the ideology of the proposal is obviously linked to the concept of CSR and voluntary, soft self-regulatory trends.

The European Commission's Green Paper, *Modernising labour law to meet the challenges of the 21<sup>st</sup> century* ("Green Paper") also takes note of subcontracting and it states that several Member States have sought to address such problems by making principal contractors responsible for the obligations of their subcontractors under a system of joint and several liability. According to the Green Paper, in line with our reasoning about the soft law connections, such a system encourages principal contractors to monitor compliance with employment legislation on the part of their commercial partners.<sup>38</sup> The outcome of the public consultation on the Commission's *Green Paper* encouraged in this regard the Commission's intention to take the necessary steps to clarify the rights and obligations of the parties involved in subcontracting chains to avoid depriving workers of their ability to make effective use of their rights.

As far as the EU is concerned, it is important to note that the Court of Justice acknowledges the legitimacy of such national measures in general. In the case of *Wolff & Müller*, the ECJ held that the German national liability scheme did not infringe Community law but was, instead, intended to ensure the protection of workers posted abroad.<sup>39</sup> However, in another case, the Belgian joint liability scheme for (wage) tax debts was deemed to be disproportionate and thus incompatible with the Treaty provisions on the freedom to provide services.<sup>40</sup>

The European Commission conducted a study with the University of Edinburgh Law School on the 'existing legal framework for human rights and environmental issues applicable to European companies operating outside the EU'.<sup>41</sup> The final report was published in November 2010 and also analyses how labour laws can address corporate violations of human rights both within and outside the corporation (i.e. supply chain and subcontracting relationships).

On the EU level the *European Coalition for Corporate Justice* (ECCJ) put forward ambitious legal proposals to improve corporate accountability for human rights abuses in complex corporate structures. Among others, these proposals comprise the

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<sup>37</sup> Amon (n 18) 234.

<sup>38</sup> *Commission Green Paper on Modernising Labour Law to Meet the Challenges of the 21st Century*, at 3, COM (2006) final 708 (Nov. 11, 2006).

<sup>39</sup> Case C-60/03, *Wolff & Müller GmbH v. Felix*, 2004 E.C.R. I-9553.

<sup>40</sup> Judgment of 9.11.2006, case C-433/04, *Commission v Belgium*.

<sup>41</sup> <http://www.law.ed.ac.uk/euenterpriseslf/> (Last visited: 31.05. 2013.)

enhancement of direct liability of parent companies and the establishment of a parental company duty of care.<sup>42</sup>

If we take a look at *academic proposals* as well, we can find even more ambitious and brave concepts, especially in Anglo-Saxon scholarship. Albeit these proposals are originally framed for a specific national setting, their ideas are generally valuable. For instance, one conceptualization of the issue relates to the so-called ‘entrepreneurialism’ theory which focuses on determining who exercises entrepreneurial control over the work and has significant entrepreneurial opportunity for gain or loss.<sup>43</sup> Rogers takes another view and he argues for a broad duty-based approach to accountability, as he proposes that end-user firms ought to be liable for failing to exercise reasonable duty of care in preventing violations of labour laws in their supply chains regardless of whether they have contractual relationship with the primary wrongdoer.<sup>44</sup> Glynn goes one step beyond as he argues for the idea of a broad and true enterprise liability. He states that one promising way to counteract the compliance-reducing effects of disaggregation is to eliminate the “employer” coverage limitation of labour law altogether. He proposes that commercial actors (end-users) would be held strictly liable for some labour law violations in the production of any goods and services they purchase, sell, or distribute, whether directly or through intermediaries. In other words, accountability would extend through the commercial enterprise, unlinked from the exercise of control over the work. The only limitation is that a firm would be liable only for the portion of the violations attributable to the goods or services it purchases, sells, or distributes.<sup>45</sup> Furthermore, ideas about the so-called functional re-conceptualization of the legal notion of the employer are also underpinning the concept of shared employers’ liability in subcontracting networks. This functional-typological conceptualisation of the employer is transcending the ‘binary divide’ of the employment relationship in increasingly complex scenarios. These ideas are identifying the employer according to a ‘functional’ test (e.g. based on the level of control), not only via the formal legal relationship.<sup>46</sup>

## 5. National hard law measures

State intervention into the labour market, as the fundamental pillar of labour law can take many forms. Hard law measures might gain inspiration from the above described CSR, soft law and self-regulatory practices. Although joint liability laws in subcontracting chains have some sporadic history in some countries (e.g. from the

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<sup>42</sup> For details see: Proposals for ‘Enhancing Direct Liability of Parent Companies’ and for ‘Establishing a Parental Company Duty of Care’, *European Coalition For Corporate Justice (ECCJ) Legal Proposals to Improve Corporate Accountability for Human Rights Abuses* (2008).

<sup>43</sup> Cf. Harper, Michael C., ‘*Defining the Economics Relationship Appropriate for Collective Bargaining*’ (1998) 39 B.C.L. Rev. 329, <http://lawdigitalcommons.bc.edu/bclr/vol39/iss2/2>

<sup>44</sup> Rogers, Brishen, ‘*Toward Third-Party Liability for Wage Theft*’ (2010) 31 Berkeley J. Emp. & Lab. L. 1.

<sup>45</sup> Glynn (n 1) 105.

<sup>46</sup> See for more details: Prassl, Jeremias, ‘Rethinking the notion of the employer’, Conference Paper, Inaugural conference of the Labour Law Research Network, Barcelona, June 13-15, 2013; Fudge, Judy: *The Legal Boundaries of the Employer, Precarious Workers, and Labour Protection* (eds.: Davidov, Guy & Langille, Brian) *The Idea of Labour Law* (Oxford University Press 2011) 310-313.

1960s and 1970s in the Netherlands, Belgium, Finland, France)<sup>47</sup>, in their modern form they are relatively new in most of the European countries. According to our assumption, their emergence is in connection with and backed by the above described recent soft law developments and conceptual innovations.

Besides the above-mentioned international regulatory efforts and guidance about chain-responsibility, some countries adopted specific *national liability schemes* (Austria, Belgium, Finland, France, Germany, Italy, the Netherlands and Spain).<sup>48</sup> National schemes are very varied in their nature, scope and implementation. As for their legal nature, they are ranging from limited liability arrangements to full chain-liability systems. Furthermore, a differentiation can be made between objective liability schemes and liability schemes with possible exemptions (mostly on the basis of positive, due diligence obligations, such as reliability checks, certifications, payment guarantees). Certain aspects of labour conditions (such as wages, social security contributions, health and safety, protection of posted workers) are more common to be regulated via chain-responsibility measures than others. Similarly, certain branches of the economy (such as the construction industry, often linked to public procurement law) are usually over-represented in the scope of the respective measures than others. Furthermore, some measures cover only some, limited tiers (typically first and second levels) of the chain of contractors. On the whole, currently, there is practically no European state (or EU Member State) with an all-encompassing, extensive, well-working system of full joint and several liability. Furthermore, the majority of EU Member States (15 of the 27) have not set up any protective arrangements concerning labour law liability or responsibility other than minimally required by EU directives (see below).<sup>49</sup> In these countries the contractual relationships apply strictly, without any breakthrough on them. There are some countries with functional equivalents or alternative measures in place instead of joint and several liability, such as co-decision rights of trade unions (e.g. Sweden), social clauses in collective agreements (e.g.: especially in the Nordic countries), limitation of the subcontracting chain (e.g.: Spain) , informational obligations.<sup>50</sup>

Another possible cluster of joint liability regulation relates to *public procurement*. According to both EU-level public procurement directives and respective national regimes it is possible for public authorities to adopt or further develop legal provisions which exclude undertakings from public procurement, where they are found to have infringed labour law, collective agreements or codes of conduct in supply chains. Public procurement laws can promote responsible supply chain management on many ways.

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<sup>47</sup> Amon (n 18) 244.

<sup>48</sup> Cf. European Parliament Resolution on the social responsibility of subcontracting undertakings in production chains 26 March 2009 (2008/2249(INI)), 9. See for further details: Jorens, Yves & Peters, Saskia & Houwerzijl, Mijke, *Study on the protection of workers' rights in subcontracting processes in the European Union* (2012) Project DG EMPL/B2-VC/2011/0015, Ghent University & University of Amsterdam. Houwerzijl Mijke & Peters, Saskia, *Liability in Subcontracting Processes in the European Construction Sector* (2008) Eurofound, European Foundation for the Improvement of Living and Working Conditions.

<sup>49</sup> Jorens, Yves & Peters, Saskia & Houwerzijl, Mijke (n 48) 3.

<sup>50</sup> Jorens, Yves & Peters, Saskia & Houwerzijl, Mijke (n 48) 44.

In the *EU*, there already some fields of labour law where *Directives* provide for some kind of subcontracting regulation:

- As for health and safety matters in contracting chains, it is to some extent set out in the European legislative framework. The Framework Directive (Council Directive 89/391/EEC of 12 June 1989) obliges employers, within the context of their general obligations, to take the necessary measures for the safety and health protection of workers, including prevention of occupational risks. Similarly, Council Directive 92/57/EEC that addresses the minimum safety and health requirements at temporary or mobile construction sites (the 'Construction Sites Directive'), establishes that the client or project supervisor shall appoint one or more coordinators for safety and health matters for any construction site on which more than one contractor is present.
- As public purchasers command a large share of the market (such as in construction), their impact on their (sub-) contracting chain is significant. The current legal basis for public procurement at EU level is provided by the Procurement Directives, namely Directives 2004/17/EC and 2004/18/EC.<sup>51</sup>
- By adopting Directive 2009/52/EC on sanctions and measures against employers of illegally staying third-country nationals, the EU legislator did for the first time introduce chain liability rules in the framework of subcontracting processes. Where the employer is a subcontractor, the Directive, under certain conditions, provides for a mechanism of joint and several liability with respect to financial sanctions as well as back payments relating to outstanding remuneration; liability may also be extended to those in the subcontracting chain who knew that the subcontractor employed illegally staying third-country nationals.<sup>52</sup>

Besides the above mentioned fields of EU-law, it is important to mention that the proposal for a new directive on the enforcement of Directive 96/71/EC concerning the posting of workers puts forward the idea of a joint liability provision. The current proposal contains specific provisions concerning contractors' obligations and (joint and several) liability with respect to compliance with the relevant terms and conditions of employment of posted workers by subcontractors (Article 12.). The focus is on preventive measures (risk-based due diligence when selecting subcontractors), combined with the possibility for Member States who so wish to maintain or

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<sup>51</sup> In the contract documents, the contracting authority may ask or may be required by a Member State to ask the tenderer to indicate in his tender any share of the contract he may intend to subcontract to third parties and any proposed subcontractors. However, this indication shall be without prejudice to the question of the principal economic operator's liability. See: Article 25 of Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts.

It is noteworthy, that the proposal for the new directive on public procurement contains slightly more elaborated rules on subcontracting. For instance, it provides for the direct payment of subcontractors in as much as Member States can provide that subcontractors may request for direct payment by the contracting authority of supplies, works and services provided to the main contractor in the context of the contract performance. This offers subcontractors which are often SMEs an efficient way of protecting their interest in being paid. See: Proposal for a Directive on public procurement, COM/2011/0896 final - 2011/0438 (COD), Article 71.

<sup>52</sup> Jorens, Yves & Peters, Saskia & Houwerzijl, Mijke (n 48) 5.

implement more far-reaching systems of joint and several or chain liability. The proposed system of joint and several liability is limited to direct subcontractor situations in the construction sector where most of the cases of non-payment of wages have been reported. Contractors which have undertaken due diligence obligations cannot be held liable. Posting by temporary work agencies is included provided it is aimed at activities in the construction sector. However, Member States may, if they so wish, extend these provisions to other sectors.<sup>53</sup>

Also in the *US* there are innovative legal solutions which try to extend responsibility beyond employers. Among the notable examples are the federal level FLSA's (Fair Labor Standards Act) so-called 'hot goods' provision<sup>54</sup> and some state-level laws, such as the California's 'brother's keeper' law. The latter holds user firms in certain low-wage industries responsible for subcontractors' wage and hour violations under a duty-based standard.<sup>55</sup>

It is important to underline that the factual *effectiveness* of existing hard law mechanisms, notably joint and several liability and chain liability schemes is often debated and called into question. In spite of their existence, in some countries they are clearly labelled as overly onerous and ineffective (mostly because of their complicated nature and enforcement problems). Conversely, their most often referred to positive feature is rather soft and indirect: at best, such rules can have preventive and deterrent impact on the behaviour of main contractors to motivate them to choose their subcontractors more diligently.<sup>56</sup> Another ambiguity ('softness') of such laws lies in the fact that it is unclear to what extent a transposition can be made from a mechanism applicable in a national context to a broader European or international context. An additional related procedural difficulty is that it is often the workers themselves who have to take the initiative to enforce their rights under subcontracting laws. This may be especially challenging in cross-border situations, since foreign workers are even more unable or reluctant to stand up for their rights.<sup>57</sup> On top of that, such legislative developments are often depicted as soft laws in a sense that they shift public inspection and enforcement duties on private entities.<sup>58</sup>

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<sup>53</sup> Proposal for a Directive on the enforcement of Directive 96/71/EC concerning the posting of workers in the framework of the provision of services, COM/2012/0131 final - 2012/0061 (COD).

<sup>54</sup> One way the Fair Labor Standards Act (FLSA) seeks to ensure compliance with the law's minimum wage, overtime, and child labor statutes is to prohibit employers from shipping, delivering, or selling in commerce any goods produced in violation of the federal wage and hour requirements. This FLSA prohibition is called the "hot goods" provision, and it enlists companies in the whole supply chain — from raw goods producers to manufacturers to retailers — in ensuring compliance. So even if an employer pays its own employees in accordance with the federal wage and hour requirements, if it has knowledge that companies from which it obtains goods do not comply, it can be held responsible. <http://www.hrwebadvisor.com/headlines/article/flsa-hot-goods-garment-industry-administrative-subpoena> (05.09. 2013)

<sup>55</sup> For further details, see: Glynn (n 1) 104. Also in California, The California Transparency in Supply Chains Act of 2010 (SB 657) went into effect January 1, 2012. This law requires large retailers and manufacturers that do business in the state of California, and that have gross worldwide sales of over \$100 Million Dollars, to be transparent about the efforts they have undertaken to eradicate Slavery and Human Trafficking in their supply chain.

<sup>56</sup> Amon (n 18) 247-255.

<sup>57</sup> Jorens, Yves & Peters, Saskia & Houwerzijl, Mijke (n 48) 158.

<sup>58</sup> Jorens, Yves & Peters, Saskia & Houwerzijl, Mijke (n 48) 157.

Nonetheless, these national regulatory ‘experimentations’ are promising in the sense that they try to ensure the protection of workers’ rights in subcontracting processes. As we have already pointed out, the legal idea that principal contractors (or hub companies) should be responsible for (some of) the labour law obligations of their sub-contractors is in close relation with the corporate accountability and CSR movement.

## 6. Conclusions - Convergence of soft law and hard law

In regulating labour issues along supply chains there is a clear dichotomy between soft law / self-regulatory and hard law measures: there are some embryonic hard law measures (mostly on the national level) and a plethora of voluntary, self-regulatory RSCM mechanisms (mostly on the transnational level, developed by TNCs).

There is a detectable convergence between these soft and hard measures. On the one hand, transnational soft law measures (voluntary RSCM practices of TNCs) can be seen – directly or at least indirectly - as antecedents, patterns and inspiration for hard law proposals and, to some extent, for national liability schemes. On the other hand, most of the hard law proposals and existing national measures are, either explicitly or only implicitly, motivating private self-regulation, since their effectiveness and success is largely dependent on the proactive attitude of the regulated actors, and on the ‘soft’-like behavioural- and attitude-control effects of legislative measures. All in all, there is an existing and much needed mutuality and concentricity between self-regulation and regulation, or soft law and hard law in the field of regulating working conditions in subcontracting networks. This is a field of hybrid regulation<sup>59</sup> where, on the one hand, pure soft laws are certainly not enough (because of the harshly conflicting business and social interests). However, on the other hand, hard laws can’t be truly effective by imposing overwhelming bureaucratic burden on ordinary economic processes such as subcontracting. In other words: too rigid hard laws for chain-liability are not just ineffective, but inconsistent with usual economic logics and thus politically unrealistic. Hence, there is a clear need for designing more hybrid legal solutions responsively combining hard and soft approaches. When regulating working conditions in supply chains, soft laws usually end up in some form of ‘harder’ solutions (such as contractual obligations in supplier contracts or in IFAs), while hard laws can’t be ‘too hard’, and they should leave room for the potential of proactive private ordering. By prompting commercial actors at risk of liability via hard laws, they are becoming motivated for effective, affirmative private ordering in terms of selecting decent suppliers. As a consequence, we argue that although new hard, legislative measures are suggested in the field of chain-liability (both on a transnational and national level), they can’t detach from reality. Such hard laws must build on the lessons already learned in private, voluntary RSCM practices, and they must combine hard and soft regulatory attitudes by relying on and spurring self-regulation to a great extent (triggering self-regulation is crucial, since it can put into place monitoring and other methods to implement compliant practices in subcontracting networks).

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<sup>59</sup> Cf.: Mückenberger, Ulrich, ‘Hybrid Global Labour Law’, In: (Roger Blanpain & Frank Hendrickx eds.), *Labour Law Between Change and Tradition, Liber Amicorum Antoine Jacobs* (2011), Kluwer.

Another reason why it is important to coordinate subcontracting-related hard and soft laws is their slightly different focus. On the one hand, soft laws (such as RSCM practices) usually try to enforce a wider range of basic labour standards along supply chains (for instance, as described in corporate policies, codes of conduct or IFAs). As such, they are rather focused on substantive and ‘enabling’ rights (e.g. freedom of association, collective bargaining, freedom from discrimination). On the other hand, hard laws (such as national liability schemes) are only targeted on some core, rather easier quantifiable and assessable labour issues (such as wages, health and safety standards, taxes and contributions). As such, they are rather focused on administrative measures.

It also goes without saying that the various social actors (such as NGOs, trade unions, some governments) are generally favouring more stringent, harder regulations of subcontracting, while the business sector is generally favouring softer regulations, if any (since they perceive subcontracting laws as having negative impact on economic performance). Consequently, only a sound combination of hard and soft attitudes can reconcile the contradictory interests.

We are convinced that no single legal panacea can fully effectively address the labour law-related problems stemming from subcontracting, as subcontracting is simply an ordinary economic technique in modern times, and law can’t go straight against economic realities. Both soft and hard measures can play a role in rebuilding the responsibility in relation to subcontracting and reconnecting power with responsibilities. In effect, we argue that soft and hard measures can be balanced, mutually reinforcing and complementary to each other and their synergies and coordination should be enhanced more strategically. Nevertheless, the overall rationale that the ultimate beneficiary of an economic activity should bear at least some part of the responsibility for working conditions in subcontracting networks is more than compelling and guiding for labour law reforms. However, any regulatory attempt, either hard or soft, should be aware of the fact that how difficult is it to put a social dimension into subcontracting transactions of a pure economic nature.