PARLIAMENTARY JOINT STATUTORY COMMITTEE ON CORPORATIONS AND SECURITIES

INQUIRY INTO CORPORATE CODE OF CONDUCT BILL 2000

submission by

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1. Introduction

Area of expertise

1.1 I am a Senior Lecturer at the University of Melbourne Law School. I am a member of that School's Centre for Employment and Labour Relations Law and of its Asian Law Centre. My relevant area of expertise is comparative labour law, particularly labour law in East Asia. I am also interested in contemporary regulatory theory as it applies to working conditions. I am currently Chief Investigator in a project on corporate codes of conduct and labour standards, funded by a large Australia Research Council grant.

1.2. In light of my background, this submission addresses those parts of the Bill which concern labour standards.

1. 3 I support the concept of using federal legislative power to encourage Australian corporations to improve labour conditions in their overseas operations. However, I believe that the Bill should be fundamentally amended. In this submission, I will:

- explain why such legislative intervention is, in principle, constructive;
- identify significant flaws in the current draft of the Bill; and
- suggest an alternative regulatory approach upon which the Bill could be based.

2. The inadequacies of private/voluntary regulation

Serious labour abuses occur in the context of globalisation

2.1 The liberalisation of goods and capital flows has clearly brought significant economic benefits to many people in the world. However, as Senator Bourne correctly points out in her second reading speech, 'globalisation' has also contributed to egregious labour abuses. This is not a reason to oppose liberalisation *per se* but it is a reason to consider responsive governmental intervention. Unquestioning acceptance of the status quo amounts to a refusal to use human ingenuity to relieve gross suffering.

Whether regulation is effective is an empirical question

2.2 However, policy responses to globalisation based on public intervention are

frequently attacked as counterproductive 'political' interference in market relations. This attack is misconceived since, as John Braithwaite and Peter Drahos convincingly demonstrate, the regulatory structure enabling economic globalisation is itself a highly political form of 'interference'.[1] Whether any particular form of regulation is effective or not is, therefore, essentially an empirical question. There is already a rich empirical literature suggesting which forms of regulation may be suitable in given contexts.[2] This submission is informed by that literature.

The strengths of private codes of conduct

2.3 Some opponents of governmental intervention on labour issues advocate the use of private forms of regulation (or 'self-regulation'), such as 'voluntary' codes of conduct. Three major advantages of voluntary codes of conduct, vis-à-vis 'command and control' regulation are their internalisation of enforcement, their flexibility - they allow for 'rolling standards' - and their capacity to reach across borders into sub-contracting chains, far beyond the scope of domestic regulation in a firm's home country.

The weaknesses of private codes of conduct

2.4 On the other hand, voluntary codes of conduct suffer several deficiencies as mechanisms for promoting labour standards.[3] First, in the absence of effective sanctioning mechanisms, many firms will have little incentive to establish meaningful codes. Firms are generally led to adopt private codes in response to public pressure but this pressure is weak in many instances, particularly in respect of firms which produce intermediate rather than consumer goods. Some firms do not adopt codes at all. Others may offer disingenuous sops, public relations exercises reflecting no genuine commitment to improving working conditions. Such codes are so vaguely worded as to be devoid of obligations that can be evaluated or enforced.

2.5 Second, codes vary considerably from each other so that it is difficult to compare relative performance between firms.

2.6 Third, in the absence of effective supervision, private codes lack credibility.

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[1] John Braithwaite and Peter Drahos, GLOBAL BUSINESS REGULATION, Cambridge University Press, Cambridge (2000)

[2] In addition to the authors cited elsewhere in this submission, important contributions to regulatory theory have been made, *inter alia*, by the Oxford Socio-legal scholars, Simon Deakin and colleagues at Cambridge University and the more sophisticated law and economics scholars in North America.

[3] For empirical studies see, *inter alia*, Jill Murray, *Corporate Codes of Conduct and Labour Standards*, in Robert Kyloh (ed.), MASTERING THE CHALLENGE OF GLOBALIZATION: TOWARDS A TRADE UNION AGENDA, International Labour Organization, Geneva (1998); 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 & POLICY INTERNATIONAL BUSINESS. 111 (1998) 114-119; Lance Compa and Tashia Hinchliffe-Darricarrere, *Enforcing International Labor Rights through Corporate Codes of Conduct*, 33 COLUMBIA. JOURNAL OF . TRANSNATIONAL LAW. 663 (1995); Lisa Balthazar, *Government Sanctions and Private Initiatives: Striking a New Balance for U.S. Enforcement of Internationally-recognized Workers' Rights*, 29 COLUMBIA. HUMAN. RIGHTS. LAW. REVIEW. 687 (1998) 716-721.

Some firms do not establish external systems of monitoring. Even where there are such systems, the monitors may not be adequately trained or familiar with local conditions. In some instances, their independence may be compromised by financial linkages with the firm they are supervising. Moreover, monitoring systems are diverse and fragmented; there may be no common basis for evaluation methods. This compounds the difficulty of assessing the relative performance of firms.

2.7 Fourth, codes and monitoring systems may conflict with a domestic legal system.

2.8 Finally, codes are often drafted, and monitoring systems established, without reference to the local communities to whose workers they are intended to apply. They may therefore not be responsive to the particular needs of those local communities.

2.9 For these reasons, leaving labour standards to be determined by voluntary codes alone will fail to promote better working conditions in many cases. The available evidence suggests that there is an important role for public regulation in promoting transparency and appropriate evaluation and monitoring of labour standards.

3. Is the Bill an appropriate form of public regulation?

3.1 I commend the Australian Democrats for their creative initiative in seeking to improve labour conditions through public regulation. However, this initiative unfortunately has several flaws.

Reach

3.2 Sections 8, 9 and 10 of the Bill generally apply solely to employees of an overseas corporation (sub-sections 9(1) and (2) constitute a limited exception). There is some evidence, at least in East Asia, to suggest that workers in developing countries directly employed by corporations based in the 'advanced' economies are usually *better off* than workers employed by domestic businesses. This is often because those corporations tend to employ more highly skilled workers and operate in relatively modern, well-equipped facilities. Domestic businesses are, however, usually linked to the overseas corporations through complex sub-contracting chains.

3.3 Given these circumstances, the proposed provisions will fail to reach the most vulnerable workers. Indeed, they may be counterproductive in that the overseas corporations may seek to offset any increased costs resulting from the legislation by pressuring sub-contractors to lower prices. Sub-contractors may compensate by driving their labour costs down.

Illegality in the foreign legal system

3.4 Some of the obligations imposed on overseas corporations by the Bill require

them to commit acts which may be illegal or impossible in several East Asian states. For example, section 9(3)(d) requires an overseas corporation to 'respect the rights of its workers to organise independently and bargain collectively'. Section 9(3)(f) reinforces this by requiring an overseas corporation to comply with ILO Conventions 87 and 98. If by 'independent' trade unions, the provisions mean 'independent from the state', then this provision conflicts with article 11 of the Trade Union Law of the People's Republic of China,[4] which requires Chinese trade unions to observe democratic centralism and operate under the leadership of the communist All China Federation of Trade Unions.

3.5 Again, sub-section 10(1) contains an anti-discrimination provision similar to that found in many Australian jurisdictions. However, how is it to be applied in nations where certain political opinions are banned, where laws prohibit women from working in certain industries, where homosexuality is illegal and/or where certain races are systematically favoured under the national constitution?[5]

3.6 One response to this problem would be to require overseas corporations to disinvest from countries whose laws do not comply with ILO standards. I do not favour such a requirement. Not only would it demand massive disinvestment from the region (which corporations are hardly likely to accept) but it also might well leave many workers much worse off.

Failure to consult with workers affected

3.7 This Bill appears to assume that its standards are desired by, or at least will benefit, the workers to whom it is intended to apply. However, this is a problematic assumption to make in relation to several of the standards. In the absence of consultation with those workers, we cannot know what their preferred choice of working conditions would be.

3.8. For example, the Bill requires an overseas corporation to pay a 'living wage' (s. 9(3)(a)) which is defined as 'a wage sufficient to meet the basic needs of a family of two adults and three children in the country or region they are resident in' (s. 6). However, if a young single worker wished to receive lower wages in exchange for lower hours, or to permit greater employment in her or his area, why should the corporation be prevented from agreeing? I find this aspect of the Bill somewhat paternalistic, even though it is well intended. Indeed, it seeks to impose more prescriptive standards than those applicable in Australia itself.

3.9. I do not believe this objection is overcome by arguments that the conditions in the Bill are based on international labour standards. While I do not reject the notion of international labour standards, they do need to be applied very carefully in non-Western contexts. I say this not because I accept spurious and self-serving 'Asian values' arguments, but because those standards were generally formulated by

[4] See generally, Sarah Biddulph and Sean Cooney *Trade Union Law in the People's Republic of China* (1993) 19 MELBOURNE UNIVERSITY LAW REVIEW 253-292

[5] Malaysia is an example of a society where all four circumstances prevail.

Europeans with European conditions in mind. [6] They cannot be applied in a straightforward manner in many non-European societies.

Failure to draw on the capacity of corporations to devise innovative labour strategies

3.10 The Bill rests on a static rather than a dynamic approach to labour standards. It does not encourage corporations to develop innovative strategies to improve labour conditions, or reward those that do. Nor does it permit labour standards to be revised upwards in light of these innovations.

3.11 More generally, the Bill does not seek to utilise the potentially positive aspects of self-regulation identified at 2.3: the internalisation of enforcement, the generation of flexible and contextually appropriate standards, and the ability to reach down the sub-contracting chain.

3.12 In sum, this Bill is too rigid. However, it does not of course follow that public regulation of the overseas operations of Australian corporations is undesirable. What follow is that a different kind of public regulation is required.

4. A public/private mix: Flexible standards, transparent monitoring

New forms of regulation: Ratcheting labour standards

4.1 One of the more exciting developments in regulation is the combination of private and public forms of regulation to achieve effective outcomes.[7] For example, Charles Sabel, Dara O'Rourke, and Archon Fung have proposed a system of 'ratcheting labour standards (RTS).[8] They argue that labour standards can be improved (ratcheted up) if firms are permitted to develop their own codes and monitoring systems *on the condition that* they made their results subject to public evaluation, *inter alia* through independent, accredited organisations. These organisations would systematically compare the performance of firms with each other and, in some cases, rank them. This would create an incentive structure in which firms would vie with each other for continuous improvement. It would also greatly improve the availability of information on conditions in the labour market.

4.2 This RTS scheme has several advantages over both voluntary regulation and the public regulation proposed in the Bill.

Advantages of RTS over self-regulation

4.3. The RLS framework addresses many of the deficiencies in voluntary codes. It:

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[6] See Sean Cooney, Testing Times for the ILO: Institutional Reform for the New International Political Economy (1999) 20 COMPARATIVE LABOR LAW AND POLICY JOURNAL 365-399.

[7] See Michael C. Dorf and Charles F. Sabel, *A Constitution Of Democratic Experimentalism*, 98 COLUM. L. R. 267 (1998); Charles Sabel, Archon Fung, Bradley Karkkainen, *Beyond Backyard Environmentalism*, BOSTON REVIEW, (October- November, 1999). For a somewhat different approach, see Hugh Collins, REGULATING CONTRACT , Oxford University Press, Oxford, 1999.

[8] Charles Sabel, Dara O'Rourke, and Archon Fung, *Ratcheting Labor Standards: Regulation for Continuous Improvement in the Global Workplace*, paper prepared for World Bank; last amended February 2000, available at http://www.law.columbia.edu/sabel/papers.htm.

- obliges firms to be more transparent and accountable in their social audits and to compare their performances;
- permits independent assessment of whether firms have complied with their codes; and,
- permits public debate on the appropriateness of the codes, including scope for NGO's to challenge the claims of firms about the content of, and their compliance, with their codes.

4.4 RTS also has advantages over the model of public regulation upon which the Bill is based. It:

- better harnesses principles and mechanisms characteristic of contemporary corporate behaviour, requiring firms to prove their claims about 'transparency', 'continuous improvement' and 'world's best practice';
- fosters a dynamic approach to labour standards – a 'race to the top' and mutual learning;
- enables firms to adapt their practices to the local environments, since it is not necessary that the standards be the same in all places.

4.5 While RTS represents a radically different approach to regulation, it is based on empirical analysis of successful regulatory experiments currently in operation, particularly in the United States.[9]

Participation by workers affected

4.6 I have certain reservations about the RTS model. In particular, as currently formulated, it gives insufficient emphasis to the opinions of the workers affected by codes. This may be remedied by requiring corporations to consult adequately with their employees (and, if possible, sub-contracting workers) in preparing their code.

Applying RTS in Australia: Modifications to Part 3 of the Bill

4.7 I suggest that the Bill be reworked to implement a system that is founded on the main principles of RTS.

4.8 The Bill already contains the core of the RTS idea in its Part 3 reporting requirements but it focuses on punishing contravention of fixed standards rather than encouraging upgrading. This should be modified so as to provide that overseas corporations report to a designated agency on the measures they have devised to improve labour conditions. The agency would publicise the information and assess the corporations' performance. The system would be somewhat analogous to the audits conducted under the Equal Opportunity for Women in the Workplace Act 1999 (Cth).

[9] See references at note 7.

Criteria for assessing performance

4.9 The precise criteria of the audit should be determined by the designated agency. Core labour standards would provide initial guidelines for evaluation but more specific benchmarks could be developed by the agency from year to year in light of information it receives from corporations about feasible improvements.

4.10 It may be desirable to have develop different criteria in order to respond to divergent national and industry conditions. However, the central idea would be to structure the assessment around the extent to which the overseas corporation has succeeded in implementing or improving upon international labour standards *relative to its previous performance and to the performance of similar corporations.*

Reach of assessment

4.11 The assessment of a corporation need not be based on its treatment of its own employees alone. A corporation that developed a creative strategy to improve the working conditions of its sub-contractors should be highly commended. This would help to overcome the limitations in the Bill discussed at 3.2 to 3.3.

Role of other concerned parties

4.12 The designated agency should be empowered to accept submissions from concerned persons and groups, such as employees, sub-contractors and NGO's which confirm or challenge corporation reports. In particular, representations from employees of overseas corporations or their sub-contractors should be given weight.

Designated Agency

4.13 Part 3 of the Bill requires the Australian Securities and Investments Commission to conduct audits. I am not sure that the Commission is the appropriate body. If the Commission is unwilling to undertake the monitoring and evaluating role outlined here, Parliament may wish to consider vesting another agency (such as the Australian Industrial Relations Commission) with the appropriate authority. Alternatively, appropriate private or community sector agencies could conduct the monitoring and evaluating.

Use of audits

4.14 Corporations should be able the public audits produced by the designated agency as they wish, subject to relevant Trade Practices Act provisions such as the prohibition on misleading or deceptive conduct (s. 52). For example, well-performing firms might wish to publicise their evaluations in order to gain a competitive advantage over their rivals among ethical consumers.

Further incentives to improve performance

4.15 If the public audit alone proved ineffective in upgrading labour conditions, the Parliament could consider strengthening the incentives for improved performance either through a public ranking of firms or through appropriate use of the tax system.

Wider application of the audit system

4.16 I note in passing that there is no reason why the audit system should not apply also to the Australian operations of corporations.

Parts 2 of the Bill

4.17 Given the re-orientation of Part 3, Part 2, in so far as it applies to labour standards, needs to be greatly simplified.

4.18 As explained at 3.4- 3.5, some of the standards prescribed in Part 2 may be counterproductive and/or incapable of implementation. In my opinion, a preferable approach would be to provide a very basis floor of rights, upon which corporations would be encouraged to build in an innovative, responsive way.

4.19 I suggest that the whole of the Part be deleted apart from:

- Sub-sections 8(1) and (2)(a), (b), (f) and (g); and
- Sub-section 9(3)(e) (f).

4.20 Sub-section 9(3)(f) should be amended by adding the words 'in so far as these can be implemented consistently with the laws of the country in which the overseas corporation is operating'. Although, as I suggested at 3.4-3.5, this would entail some departure from ILO standards in certain countries, this would not be, in my view, a drastic departure. East Asian labour laws, on paper at least, *generally* tend to follow ILO standards.

4.21 The definition of minimum standards in section 6 should be amended to include Convention 182 on the Elimination of the Worst Forms of Child Labour.

Part 4

4.22 I have serious reservations about the applicability of Part 4 of the Bill to labour standards. I can see the usefulness of Part 4, particularly in relation to egregious conduct. However, it will not be clear in many cases what constitutes a contravention of the obligations in the Bill given the greatly differing social, economic, political and legal circumstances in the countries in which overseas corporations operate. The Court would face severe interpretational and evidentiary problems in such cases.

5. Conclusion

5.1 The Bill, at least in so far as it seeks to regulate labour conditions, is seriously flawed. It ought not be passed *in its current form.* My concern is that these flaws will lead to a complete rejection of the idea behind the Bill. This would be unfortunate because there is an opportunity here to make an innovative and, I believe, effective contribution to improving labour conditions. However, in order for this to opportunity to be realised, the Bill should be extensively modified along the lines suggested in this submission.