



Reconciling due diligence with trade tensions

“The OECD has long been an advocate for market openness that supports sustainable and inclusive growth.” OECD Secretary General Angel Gurría¹

Discussion questions

- How important are current trade actions - in light of the long-stalled stock of trade restrictions - on supply chains in the garment and footwear sector in terms of production and trade?
- How does the shifting of supply chains affect the labour, environmental, human rights and integrity context in which companies are operating?
- What due diligence measures can companies take to address RBC risks within a context of increased uncertainty and what is the role of governments in enabling this?

Background

Economic uncertainty is the most pressing concern for firms globally.²

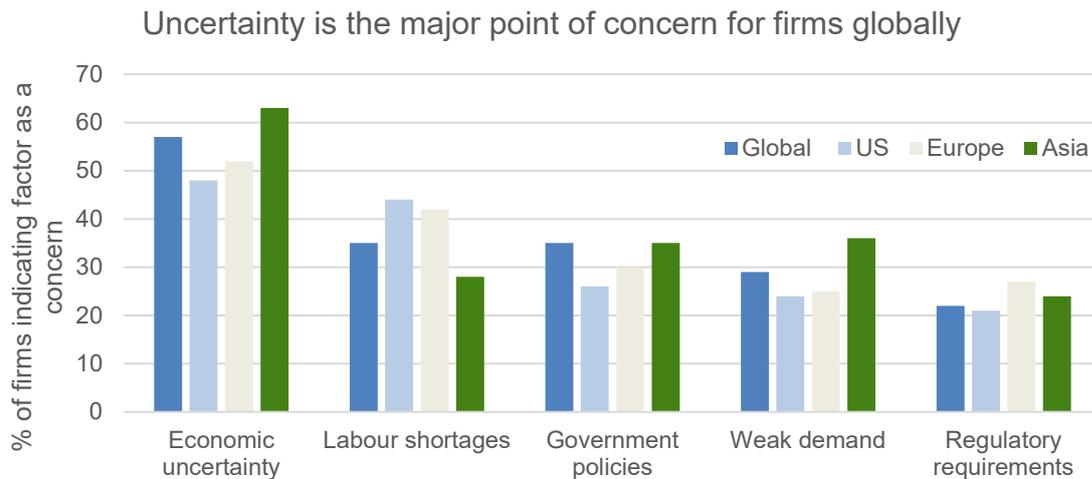
According to the OECD 2019 Economic Outlook, economic uncertainty became the most pressing concern for firms around the world in the eighteen months following the start of US-China trade tensions (Figure 1).³ With the increasing unpredictability of trade policies, high uncertainty is likely to be a persisting drag on activity for a prolonged period. While China and the United States are most affected by these shocks, all economies are adversely affected by the trade slowdown and rising uncertainty, with business investment impacted severely in the major economies.⁴

¹ Quote is within the context of the signing of the CPTPP, <http://www.oecd.org/fr/apropos/secretairegeneral/oecd-welcomes-cptpp-agreement.htm>

² OECD Economic Outlook 2019, Figure 1.2 ; Economic Outlook 106 database; Markit; OECD Main Economic Indicators database; Refinitiv; and OECD calculations. Note: Share of firms citing the factors shown as the most pressing concern of senior management over the past quarter. Based on surveys from March 2018 and September 2019. The factors shown are the ones most heavily cited globally. Firms are allowed to choose more than one factor

³ OECD Economic Outlook, Volum 2019, Issue 2, 2019

⁴ OECD Economic Outlook, Volum 2019, Issue 2, 2019



Companies operating in the garment and footwear supply chain are notably affected by the trade context between China and the United States in light of the dominant role that China plays in the sector.⁵ Tariffs on the majority of imported garment and textile goods from China to the United States increased an additional 15 percent (on top of World Trade Organisation most favoured nation rates) from September 2019⁶, before the most recent signing of the Economic and Trade Agreement between the United States and China in January 2020. Although too early to trace the total shift in production, interviews with US companies and the American Apparel and Footwear Association indicate that US based companies are taking steps to move production out of China, quickly.⁷ However, one of the primary constraints for doing so is finding sourcing destinations that can adequately absorb the demand. Interviews indicate that US companies are increasingly exploring markets that have traditionally been dominated by European buyers – such as Bangladesh – as well as new markets entirely – such as Africa.

While the US and China trade relationship took centre stage in 2019, other actions affecting the garment and footwear sector include Brexit, which resulted in considerable trade volatility across sectors in 2019, and the review of Everything But Arms EU trade preferences in Cambodia.

Trade agreements are unlocking potential new markets and market growth, while also incorporating expectations on responsible business conduct (RBC)

Regional trade agreements cover more than half of international trade today, operating alongside global multilateral agreements under the World Trade Organisation (WTO). In recent years, many countries have actively sought to establish new – and often more modern and progressive – bilateral and regional trade agreements that aim to increase trade and boost economic growth.⁸ (Figure 2) Two important trade agreements in 2019 for the garment and footwear sectors include the signing of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and the Viet Nam – EU Trade and Investment Agreements.

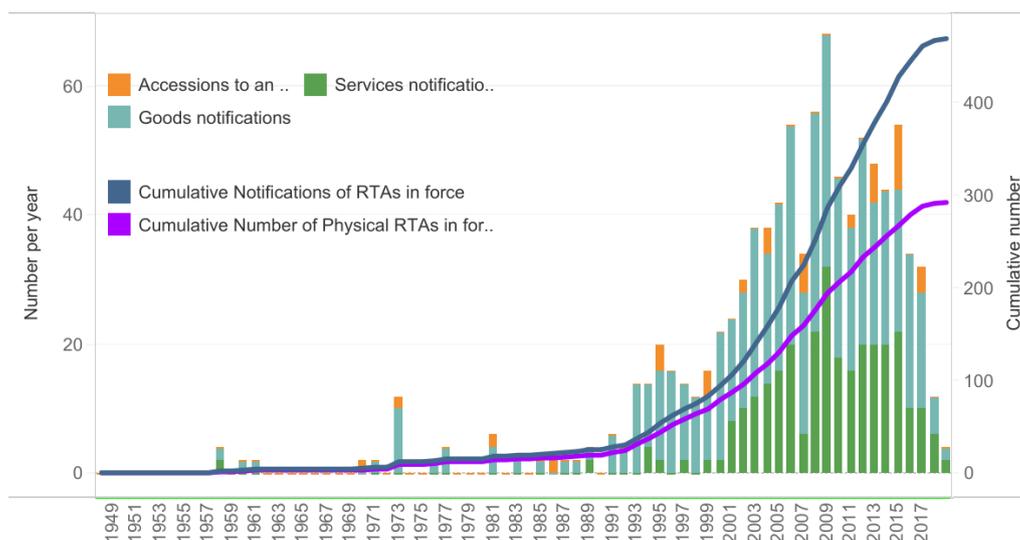
⁵ China accounts for just under 40 percent of global apparel exports.

⁶ Dr Sheng Lu, (January 2020), *US-China Tariff War – the textile and apparel hit list updated*, Just Style

⁷ The OECD Secretariat spoke with a range of US based companies and the American Apparel and Footwear Association in preparation for the OECD Forum on Due Diligence in the Garment and Footwear Sector. Such discussions were intended to provide for additional perspective and context, but do not necessarily represent the position of the entire industry.

⁸ Taken from the OECD, <https://www.oecd.org/trade/topics/regional-trade-agreements/>

Evolution of regional trade agreements over time



WTO, Regional Trade Agreements Information System (RTA-IS), Extracted on 28/01/2019, Evolution of physical RTAs

Trade arrangements are increasingly being used as a tool to promote RBC through unilateral preferences, import restrictions, and bilateral and regional trade agreements that contain labour and/or environmental provisions. For example the CPTPP includes chapters on labour, the environment and bribery and corruption.⁹ Similarly, the Viet Nam – EU Trade Agreement includes a binding chapter on trade and sustainable development, dealing with labour and environmental matters. (See *Annex: Example trade actions with RBC implications for the garment and footwear sector* for more information)

Implications on responsible business conduct

The implications of both trade tensions and newer trade agreements extend beyond demand and production levels to the RBC context in which companies are moving into or away from.

As companies seek to enter into new markets:

Conducting adequate country-level due diligence in order to understand the labour, human rights and environmental context is critical to being able to approach production responsibly. Companies should consider whether they are able to move into a new sourcing market and uphold labour, environmental and integrity standards. Moving into new markets may have an impact on the total levels of production within the country. If production cannot adjust quickly, this may result in increased rates of subcontracting, increased overtime or, potentially, increased reliance on migrant workers. Ensuring that such practices do not contribute to labour abuses in the supply chain will be important. Increased production, if not properly managed, can likewise have adverse impacts on the environment.

⁹ Access Chapter 20, Environmental of the CPTPP online, <https://dfat.gov.au/trade/agreements/in-force/cptpp/official-documents/Documents/20-environment.pdf>

As companies grow upstream production within countries:

Many free trade agreements include specific clauses on country of origin, which can provide incentives for governments and business to develop upstream segments of the supply chain. However, many upstream production processes, such as dyeing or tanning, hold greater risk of environmental harm. As such, strategically considering ways to grow the sector in a way that attracts responsible investment and the use of best available techniques will be important. As companies and countries seek to develop upstream production processes, they are also well placed to establish systems to enable traceability early on, and thus facilitate due diligence.

As companies consider whether to disengage from countries or suppliers:

The OECD Due Diligence Guidance for Responsible Supply Chains in the Garment and Footwear Sector supports continued engagement rather than disengagement to the extent possible. However, where disengagement is the only option, companies should do so responsibly. Within the context of OECD due diligence guidance, this includes complying with national laws, international labour standards and the terms of collective bargaining agreements; provide detailed information supporting the business decision to management and to the union, where one exists; and give the supplier sufficient notice of the ending of the business relations.

While uncertainty remains a dominant theme persisting into 2020, uncertainty is not new to the garment and footwear sector. In 2004, the International Trade Centre published a paper titled “Textiles and Clothing uncertainties before and after the quota phase-out”, which examined the end of the quota system for international trade in the textiles and garment.¹⁰ In 2008, companies in the apparel sector questioned the impact of the financial crisis on production and demand. As companies continue operating in uncertain times, embedding due diligence into company management systems and ways of working will be increasingly important to ensure that companies have the experience and processes in place to respond responsibly.

¹⁰ Mr. Matthias Knappe, ITC Senior Market Development Officer (Textiles and Clothing), International Trade Center, UNCTAD and WTO, http://www.intracen.org/uploadedFiles/intracen.org/Content/Exporters/Sectoral_Information/Manufactured_Goods/Textiles/Textiles%20and%20Clothing%20Uncertainties%20before%20and%20after%20the%20quota%20phase-out.pdf

Annex. Example trade actions with RBC implications for the garment and footwear sector

Signing of the Economic and Trade Agreement Between the United States of America and the People's Republic of China, 15 January 2020

On 15 January 2020 a Phase One trade agreement was signed between China and the United States. Within the context of the agreement, the United States committed to reduce punitive tariffs on Tranche 4A products from 15 percent to 7.5 percent, to go into effect in February 2020. This action reverses the tariff on apparel items imported into the US from China, which have been at a 15 percent rate since September 2019.¹¹

Signing of the Viet Nam – EU Trade and Investment Agreements, 30 June 2019¹²

The Vietnam – EU Trade Agreement includes a binding chapter on trade and sustainable development, dealing with labour and environmental matters relevant to trade relations between the EU and Vietnam.

The chapter sets specific provisions with the two-fold aim of (1) promoting mutual supportiveness between trade and investment, labour, and environmental policies, and (2) ensuring that increased trade and investment do not come at the expense of workers and environmental protection. Against this background, the chapter includes obligations from both the EU and Vietnam regarding a core set of labour and environmental issues.

With respect to labour matters, specific commitments address the effective implementation of each of the four International Labour Organization (ILO) core labour standards and of all the ratified ILO Conventions (not only the fundamental ones), as well as progress towards ratification of non-ratified fundamental ILO Conventions.

On the environment, the agreement includes commitments to the effective implementation by each Party of all the ratified Multilateral Environmental Agreements (MEAs), including, among others, the UN Convention on Biological Diversity (CBD), the UN Convention on International Trade in Endangered Species (CITES) and the UN Framework Convention on Climate Change (UNFCCC). With regard to the latter, a dedicated article on climate change further underlines the common commitment of the EU and Vietnam to achieve climate change objectives.

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¹² All information included within this section is extracted from the "Guide to the EU Viet Nam Trade and Investment Agreements, Delegation of the European Union to Vietnam, https://trade.ec.europa.eu/doclib/docs/2016/june/tradoc_154622.pdf

The agreement also establishes specific disciplines to avoid a ‘race to the bottom’ in the labour and environmental areas.

Neither the EU nor Viet Nam can derogate from, or fail to effectively enforce, any of its domestic labour and environmental laws in order to attract trade or investment. At the same time, it recognises the right of each Party to regulate in the area of labour and the environment and to establish the levels of protection it deems appropriate beyond – but not below – the commitments to ILO standards and Conventions and to MEAs. Specific attention is paid to trade and investment practices that foster sustainable development. This includes fair and ethical trade and other voluntary sustainable assurance schemes, as well as Corporate Social Responsibility (CSR), where reference is made to international principles and OECD guidelines on responsible business conduct.

The agreement establishes dedicated institutional structures to ensure the full implementation of the chapter and its oversight,

A Specialised Committee on Trade and Sustainable Development will specifically monitor the implementation of the trade and sustainable development chapter. In addition to this Specialised Committee, the chapter also foresees specialised structures for the active involvement of civil society from both sides. At the domestic level, both the EU and Vietnam will consult Domestic Advisory Groups (DAGs). DAGs will comprise independent civil society representatives and include employers’ and workers’ organisations, business groups, and environmental organisations.

Signing of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP)¹³

The Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) is a free trade agreement (FTA) between Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, Peru, New Zealand, Singapore and Vietnam.

The CPTPP includes a chapter on Labour that promote compliance with internationally-recognised labour rights, enhanced cooperation and consultation on labour issues, and effective enforcement of labour laws in CPTPP Parties.

CPTPP Parties are required to have laws governing acceptable conditions of work relating to minimum wages, hours of work and occupational health and safety. The Labour Chapter prohibits CPTPP Parties from weakening the protections afforded to workers under their labour laws, or from failing to enforce them in a manner affecting trade and investment. The Chapter also promotes initiatives to discourage the importation of goods produced by forced or compulsory labour, including child labour.

Should a dispute arise between CPTPP Parties under the terms of this Chapter, Parties must make every effort to resolve the dispute through cooperation and consultation. However, should

¹³ All information included within this section is taken from the Department of Foreign Affairs and Trade of the Australian Government, <https://dfat.gov.au/trade/agreements/in-force/cptpp/Pages/comprehensive-and-progressive-agreement-for-trans-pacific-partnership.aspx>

that process fail to resolve the dispute, CPTPP Parties may use the procedures in the CPTPP Dispute Settlement Chapter.

The CPTPP Environment Chapter aims to promote sustainable development through mutually supportive trade and environmental policies, and to achieve higher levels of environmental protection in CPTPP countries.¹⁴

The CPTPP Environment Chapter promotes the effective enforcement of domestic environmental laws and lays the foundation for CPTPP Parties to work together to address a range of trade-related environmental challenges. The Environment Chapter requires CPTPP Parties to commit to high standards of transparency and to consultation with respect to environmental laws. The CPTPP Environment Chapter includes provisions promoting the effective enforcement of CPTPP Parties' environmental laws. These include provisions to ensure that interested persons may request investigations into alleged violations of a CPTPP Party's laws, and to ensure that transparent judicial or administrative enforcement mechanisms and sanctions are available in each Party's domestic legal system.

The Chapter is subject to a robust enforcement mechanism that includes a three-step consultation process for CPTPP Parties to use in seeking to resolve any disputes that arise. If Parties fail to resolve a dispute through consultations, they may use the procedures in the CPTPP Dispute Settlement Chapter.

The CPTPP contains provisions on anti-corruption measures

The TPP Transparency and Anti-corruption Chapter requires Parties to adopt or maintain domestic provisions which criminalise (and appropriately sanction) corrupt behaviour in matters that affect international trade or investment. Such behaviour includes promising, offering or giving a bribe to a public official, as well as soliciting or accepting a bribe by a public official when committed intentionally. The CPTPP encourages Parties to promote integrity, honesty and responsibility among its public officials and to adopt a range of related measures.

The CPTPP recognizes that public and private sectors have a role to play in addressing corruption and bribery. CPTPP Parties affirm their commitment to adhere to the *APEC Conduct Principles for Public Officials* and encourage observance of the *APEC Anti-corruption Code for Business: Business Integrity and Transparency Principles for the Private Sector*. Parties are also encouraged to consider adopting whistle-blower protection laws.

Review of Everything but Arms (EBA) Trade Preferences¹⁵

Established in 2001, Everything but Arms (EBA) gives 49 of the world's poorest countries duty-free access to EU markets. EBA applies to all of their exports except for arms and ammunition and is part of the EU's wider Generalised Scheme of Preferences (GSP), which includes three sub-schemes for developing countries. EBA is conditional on compliance with the principles of 15

¹⁴ Access Chapter 20, Environmental of the CPTPP online, <https://dfat.gov.au/trade/agreements/in-force/cptpp/official-documents/Documents/20-environment.pdf>

¹⁵ All information included within this section is taken from the European Parliament, "Everything but arms, the case of Cambodia", [http://www.europarl.europa.eu/RegData/etudes/ATAG/2019/637931/EPRS_ATA\(2019\)637931_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/ATAG/2019/637931/EPRS_ATA(2019)637931_EN.pdf)

UN/International Labour Organization conventions on core human and labour rights, and can be withdrawn if there is 'serious and systematic violation' of those principles.

The European Commission launched a period of 'enhanced engagement' with Cambodia, Myanmar and Bangladesh involving intensified dialogue and monitoring. For Myanmar and Bangladesh, this process is still ongoing, whereas for Cambodia, it has moved on to the next stage: on 11 February 2019, the EU launched the procedure to suspend the country's EBA trade privileges. Depending on developments in the country, the Commission has to decide by February 2020 whether or not to suspend Cambodia's EBA privileges fully or in part. Suspension would finally come into effect six months later, by August 2020.

Detention Orders (Withhold release orders) under the U.S. Tarrif Act

Section 307 of the Tariff Act of 1930 (19 U.S.C. § 1307) prohibits the importation of merchandise mined, produced or manufactured, wholly or in part, in any foreign country by forced or indentured child labor – including forced child labor. Such merchandise is subject to exclusion and/or seizure, and may lead to criminal investigation of the importer(s).¹⁶

From 2016 to 2019 the U.S. issued 13 withhold release orders, including on imports of cotton, leather and clothing.

¹⁶ Taken from U.S. Customs and Border Protection, <https://www.cbp.gov/trade/programs-administration/forced-labor/withhold-release-orders-and-findings>