Export Contracts: Incorporating Regulatory Standards To Ensure Foreign Market Access

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Presented at

Export University 2010

Session 4:

Adapting Products to Individual Markets

July 29, 2010

Sponsored By

United States Commercial Service

Mid-Atlantic District Export Council

http://www.buyusa.gov/philadelphia/exportu.html

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I. Introduction

A. *The Importance of Standards to U.S. Exporters*

Standards are Passports for Industrial and Consumer Goods to Travel Freely in International Trade - Generally, in order for U.S. exported goods to enter the stream of commerce in a given non-U.S. market once they have cleared foreign customs they must first meet benchmarked international and/or foreign standards developed and/or enforced by recognized industry-based consensus-driven standards development organizations, governmental entities charged with enforcing domestic public interest laws and/or by civil society (e.g., nongovernmental) organizations representing public stakeholders. Standards can assume the form of mandatory (regulatory/legal) or voluntary (industry or civil society) requirements, which can be embedded and/or otherwise incorporated within supply-chain contracts entered into between manufacturers, component suppliers, fabricators, formulators, processors, assemblers, distributors, shippers, licensees, etc.

Foreign Standards Benchmarking - Foreign standards benchmarking in the 21st century entails meeting not only quality, safety, technical performance and labeling specifications/metrics, *but also* environmental, health and social responsibility requirements which can be imposed by government and/or by private parties. During the past decade, foreign governments have increasingly played a more active role in standards development and enforcement at the regulatory level to ensure that products being exported into the markets which they regulate incorporate (embed) local notions of sustainable development and other cultural norms and preferences which differ from market to market. In addition, foreign governments have more actively mandated, encouraged and/or delegated to regional, national and local private standards development organizations to develop and enforce standards that implement and comply with local laws and/or regulations, especially those relating to the environmental, social and cultural aspects of sustainable development.

B. *Satisfying Mandatory and Voluntary Standards – Conformity Assessment*

U.S. exporters must ensure that their products satisfy or comply with each of the foreign substantive mandatory (regulatory) and/or voluntary requirements.

Conformity Assessment - Demonstration of product compliance in some cases may require a simple in-country registration with a governmental authority. In other instances, demonstration of compliance will entail product evaluation or testing by a government regulatory authority or by an accredited third party verifier (e.g., independent commercial laboratories or even NGO private standards developers) authorized by a foreign regulatory authority or by the U.S. exporter's customer. U.S. exporters must ensure that they receive the proper certification and accompanying mark to demonstrate their compliance with a given standard.

Conformity Assessment – defined as any activity concerned with verifying directly or indirectly the compliance of a product, service, process, system or person with relevant requirements (voluntary standards or mandatory technical regulations).

- Typical examples of conformity assessment activities are sampling, testing and inspection, evaluation, verification and assurance of conformity (supplier's declaration), certification, registration, accreditation and approval as well as their combinations. See *ISO/IEC Guide 2, 'General terms and their definitions concerning standardization and related activities'*.

C. *Examples of U.S. and Foreign Entities Charged with Conformity Assessment*

- Underwriters Laboratories (UL); ASTM; ASME – certification & testing - issues marks – (private industry).

- U.S. Green Building Council (USGBC) (a private membership-based nonprofit organization) – developed Leadership in Energy & Environmental Design (LEED), an internationally recognized multi-level green building certification system comprising six standards covering all aspects of the development and construction process – issues USGBC-LEED mark.

- Canadian Standards Association (CSA) Int'l – (chartered by Canadian Government).

- China National Regulatory Commission for Certification and Accreditation - (government is responsible for all certification and accreditation matters – issues China Compulsory Certification (CCC) mark).

- European Telecommunications Standards Institute (ETSI), the European Committee for Standardization (CEN), the European Committee for Electrotechnical Standardization (CENELEC) – (European standards organizations developing industry-based as well as government mandated standards – issues CE mark (*Conformité Européne*) certifying conformity to such EU standards – which reflects that a product meets essential health, safety and performance requirements by design or testing.

- Japanese Standards Association (mandatory - chartered by government is responsible for standards development – works with government chartered Japanese Industrial Standards (JIS) Committee on standards certification and testing – issues JIS mark.)

- Normas Oficiales Mexicanas (mandatory - government standards development, certification, testing – issues NOM safety mark for regulated products - Certificate of Conformity issued only by accredited laboratories in-country to individuals or entities with a taxpayer number and domiciled in Mexico).

Generally speaking, the greater or more extensive the potential environment, health or safety hazard, which is typically determined by reference to a product's intrinsic characteristics, the more likely that an evaluation of a manufacturer's or supplier's quality management system and/or third party laboratory testing and certification will be called for to ensure conformity assessment. Where a product engenders a potentially significant environmental, health or safety hazard, a conformity assessment determination will be performed by governmental regulatory body or be delegated to authorized particular accredited third party certifiers and overseen by government. The more minimal the hazard, the more likely conformity assessment will be required by the manufacturer or by the U.S. exporter's purchaser or even the end-user/public stakeholder.

II. Examples of Foreign Regulatory Standards Governing Product Market Access

Increasingly, foreign government regulators are imposing on their domestic product manufacturers and suppliers and on their global supply-chain members, including U.S. and other foreign product exporters, very stringent requirements to ensure that their products are not only safe and reliable, but also do not engender environmental, health or safety (EHS) (as opposed to risks) for either the product's user and/or for society at large.

A. *European Union Regulations*

- **EU RoHS Directive** – Restriction on Hazardous Substances – restricts the use by manufacturers in electrical and electronic equipment of hazardous substances including lead, cadmium, mercury, hexavalent chromium, polybrominated biphenyls (PBB) and polybrominated diphenyl ethers (PDBE). RoHS applies to: household appliances, consumer equipment, flame retardants, information technology and telecommunication equipment, lighting equipment, electrical and electronic tools (with the exception of large-scale stationary industrial tools), toys, leisure and sports equipment, and automatic dispensers.

- **EU WEEE Directive** – Waste Electrical and Electronic Equipment – requires manufacturers to finance the collection, recycling and reuse of electrical and electronic equipment waste, and then, the removal of plastics containing brominated flame retardants and printed circuit boards from such equipment prior to recovery and recycling. Removal of plastics is not necessary if manufacturers can ensure 'environmentally safe treatment' – i.e., brominated flame retardants need not be separated if they are treated in downstream recovery or in thermal metallurgical treatment processes with appropriate off-gas treatment or are disposed in licensed landfills.

- **EU REACH Regulation** – Registration, Evaluation, Authorization and Restriction of Chemicals - REACH is a complex, three-level, volume-based system that mandates the registration of over 30,000 existing toxic chemicals presumed to be hazardous. The hazard of a substance or mixture is the potential for that substance or mixture to cause harm. It depends on the intrinsic properties of the substance or mixture. REACH also requires evaluation of

substances which 'give rise to a particular concern' and authorization for substances deemed to be 'of high concern'. REACH imposes on companies operating throughout multiple industry sectors in multiple countries up and down global product supply chains a broad legal duty of care, satisfaction of which requires compliance with an extensive pre-market authorization and information sharing process that requires registration of substances imported on their own or in mixtures and disclosure of proprietary company data within supply-chain dossiers, arguably, without adequate protection of intellectual property. Non-EU suppliers may appoint an 'only representative' (OR) to carry out registration and other importer obligations on their behalf. Consequently, importers covered by an OR registration need not register a second time and are relieved from CLP notification. OR-covered non-EU suppliers must make sure that that their substances are registered in time with regulatory deadlines taking into account all their actual and intended uses by downstream users, and also that CLP classification and labeling is undertaken.

- See *ECHA Adds Eight Substances to the Candidate List for Authorisation*, European Chemicals Agency Press Release ECHA/PR/10/12 (June 18, 2010), at: http://echa.europa.eu/doc/press/pr_10_12_candidate_list_20100618.pdf , bring the total to thirty-eight.

- On June 18, 2010, the European Chemicals Agency (ECHA) added eight new substances to the Candidate List, bringing the total to thirty-eight.

- Example of Industry Response to REACH:
  - Rolls Royce's head of supplier engineering wrote to suppliers during May 2010 "warning them of the possibility of 'severe disruptions' to its production as a result of problems in implementing the [REACH] regulations…The managing director of Indestructible Pain of Birmingham, a maker of specialist coatings for industries ranging from cars to aerospace and home fittings, called REACH a 'nightmare' for much of European manufacturing" and "would make it harder to obtain the specific chemicals needed for its paints…After November 30, 2010, it will be illegal to sell any chemicals covered by the first phase of the rules that have not been registered with the European Chemicals Agency…Rolls Royce [like] General Electric and Pratt & Whitney…is sucked into REACH because it relies on thousands of often highly specialized chemicals that are used in producing the 15,000 parts in an engine. Only a few of these chemicals are used directly by Rolls Royce. Most of them are bought or made by their suppliers, or the suppliers to these companies, and are embedded in the materials or components assembled or made by the engine maker…For REACH to succeed, companies such as Indestructible, which sells Rolls Royce in the region of 80 paints containing 140 chemicals bought from 40 suppliers, need to communicate with their customers about the nature of the chemicals inside their products". See Peter Marsh, *Rolls Royce Sounds Alarm Over REACH Rules* – Financial Times

(6/24/10) at: http://www.ft.com/cms/s/0/1ce2f620-7fc0-11df-91b4-00144feabdc0.html.

- REACH is so complex and onerous that the US Department of Commerce posted a US standards attaché at the US Mission to the European Union to help US businesses export successfully to target markets within the EU.
  - See: *Standards and U.S. Exports to the European Union*, at: http://www.astm.org/SNEWS/JA_2009/provocative_ja09.html

- REACH's requirement that industry assume "the responsibility for identifying chemical risks will…create product liability issues, particularly with respect to data generated (or not generated) and positions taken during the registration process in the EU and in other markets in which the industry participates…[that] are likely to prompt discussions between suppliers and downstream users regarding the renegotiation of supply contracts to: (1) cover the disclosure of sensitive confidential information concerning chemical composition and uses of chemicals, (2) increase prices to account for compliance costs, (3) obtain commitments from suppliers to ensure the availability of particular chemicals for particular uses in compliance with REACH, and (4) insert limitations and indemnities respecting product liability." See *EU's New REACH Regulation: A Challenge for Industry*, Hunton & Williams Client Alert (March 2007) at: http://www.hunton.com/files/tbl_s10News/FileUpload44/14156/REACH_ClientAlert_3.07.pdf .

- **EU Classification, Labeling and Packaging (CLP) Regulation** – Applicable to European companies manufacturing, importing or otherwise dealing with chemicals - substances and mixtures. The CLP regulation, based on the United Nations Globally Harmonized System (GHS), sets the rules for classification and labelling of chemicals. It aims to determine whether a substance or mixture displays properties that lead to a classification as hazardous. It sets general packaging standards to ensure the safe supply of hazardous substances and mixtures. Hazard labelling allows for the communication of hazard classification to the user of a substance or mixture, to alert the user to the presence of a hazard and the need to avoid exposures and the resulting risks. Manufacturers and importers from outside the EU must notify their classification and labeling according to CLP standards for those chemical substances and mixtures that they registered under REACH. *See*, e.g., Tim Becker, *Reach and CLP Compliance in Supply Chain 2010 – The 'Big Bang Year' For European Chemicals Industry*, CHEManager Europe (3/15/10) at: http://www.chemanager-online.com/en/topics/chemicals-distribution/reach-and-clp-compliance-supply-chain .

- **EU Energy Related Products (ErP) Directive** – Adopted October 31, 2009 and effective as of November 20, 2009. It supercedes/replaces EU EcoDesign Directive for Energy Using Products (EuP) initially adopted in 2005 and amended in 2008, which established a framework under which manufacturers of energy-using products (EuP) were, at the design stage, obliged to reduce the energy consumption and other negative environmental impacts

that occurred during the product's life cycle. "The ErP expands the scope of eco-design requirements from energy-using products (EuPs) to *all* energy-related products (ErPs). The new ErP Directive varies but little from the old EuP Directive, and will not affect the enforcement of the ten implementing measures published to date…The ten implementing measures are targeted at 10 product lots that cover household appliances (standby- and off-mode efficiency), TVs, external power supplies, etc. The ErP Directive demands more than energy efficiency. It is a framework directive aimed at covering the overall environmental impact created by a product throughout its lifetime." See *New EuP Directive 2009/125/EC Extended to Cover All Energy-Related Products*, TUVRheinland China (Dec. 7, 2009) at: http://www.chn.tuv.com/en/index.php?option=com_content&view=article&id=386:new-eup-directive-2009125ec-extended-to-cover-all-energy-related-products&catid=43:service&Itemid=76 .

- "The old Eco-Design Directive for energy using products only covered products that were using energy such as a microwave, washing machine or a television. The new ErP-Directive covers products under the old EuP Directive as well as products that are energy-related and do not directly use energy such as such as double glazing windows, taps and showerheads. According to the European Commission the definition of an energy-related product is; *'any goods having an impact on energy consumption during use'. Energy-related products include all energy-using products, plus energy-saving products such as windows and some water-using domestic devices, which can reduce water consumption and therefore the amount of energy needed to heat water."*" The ErP Directive is to be implemented in each EU Member State by November 20, 2010. See *ErP Directive 2009/125/EC (Formerly EuP)*, Intertek at: http://www.intertek.com/electrical/erp-directive/.

- "Energy-using products (EuPs) [are] products which use, generate, transfer or measure energy (e.g. electricity, gas, fossil fuel), including consumer goods such as boilers, computers, TVs, washing machines, light bulbs and industrial products such as transformers, industrial fans, industrial furnaces…Energy-related products (ErPs)…do not necessarily use energy, but have an impact on energy consumption (direct or indirect) and can therefore contribute to saving energy, such as windows, insulation material or bathroom devices (e.g. shower heads, taps)." See Ecodesign Your Future How Ecodesign Can Help the Environment by Making Products Smarter, European Commission Directorate-General for Enterprise and Industry Brochure, accessible at: http://ec.europa.eu/enterprise/policies/sustainable-business/ecodesign/index_en.htm.

B. *Japanese Regulations*

- **Japan RoHS** - Restriction on Hazardous Substances – Comprised of fifteen ministerial ordinances that the Japanese Government amended during April 2006 in response to the EU RoHS directive (regulating six hazardous substances in electrical and electronic

equipment in the European Union). The Japan RoHS covers personal computers, unit air conditioners, copy machines, televisions, microwave ovens, dryers and refrigerators. See *What is Japan RoHS?*, RSJ Technical Consulting at: http://www.rsjtechnical.com/WhatisJapanRoHS.htm . Japan RoHS is also related to the Law for the Promotion of Effective Utilization of Resources, which during 2001, made 'Design for the Environment' (DfE) mandatory for Japanese manufacturers, retailers, purchasers and consumers. DfE focuses focuses on making continuous, incremental changes in the design of products in order to reduce the quantity of resources needed for their manufacture (at the front-end) and make discarded products easier to reuse and recycle (at end-of-life) (i.e., it is akin to Europe's life cycle management.) See *What is Japan's Design for the Environment?*, RSJ Technical Consulting at: http://www.rsjtechnical.com/WhatisJapanDfE.htm .

C. *Korea Regulations*

- **Korea RoHS** - Restriction on Hazardous Substances – On April 2, 2007, the Korean National Assembly enacted the Act for Resource Recycling of Electrical and Electronic Equipment and Vehicles (Act No. 6319). The Act defines "electrical and electronic equipment" as equipment or devices operated by electric currents or electromagnetic fields – which includes electrical/ electronic equipment and vehicles. Korea RoHS includes 'Design for Environment' (DfE) in its requirements, which incorporates the Eastern value of cooperation above individualism resulting in goal-oriented regulation that reflects strong cooperation between government and producers.

  Korea RoHS imposes requirements on producers and importers of electrical/ electronic equipment and vehicles:

  - Restrictions on the use of hazardous substances;
  - Incremental improvement of materials and structure in products so that they are easy to recycle;
  - Separate collection of waste products at no cost to the person disposing of them;
  - Manufacturers/importers of electrical/electronic equipment are subject to a Mandatory Recycling Rate that is proportionate to their market share, while Producers/importers of vehicles are subject to an Annual Recycling Rate which can be fulfilled by joining a Vehicle Recycling Association;
  - Sellers of electrical/electronic equipment must provide free take-back of customer's old products and packaging materials for new products; and
  - Submission of a Recycling Requirement Implementation Plan

  "Public officials may inspect business places, facilities, equipment and documents at at any time to verify compliance with the Act. Notice is given seven days prior to the inspection except when the destruction of evidence is a concern. The Ministry of Commerce, Industry & Energy will determine compliance with hazardous materials

restrictions; the Ministry of Construction & Transportation will determine compliance with the annual vehicle recycling rate; and the MoE will determine all other compliance issues.

…The terms of the Act reflect the Korean Government's "intent to follow the precedent set by European RoHS as well as to participate in establishing future international standards." In particular, Article 7 of the Act "instructs the MoE (Ministry of the Environment) to take 'appropriate measures for international cooperation,' including mutual recognition between countries." See *What is Korea RoHS?*, RSJ Technical Consulting at: http://www.rsjtechnical.com/WhatisKoreaRoHS.htm .

- **Korea REACH** - During February 2009, the Korea Ministry of Environment ("MOE") announced new policy plans to improve the national chemical system. Generally, the new Korea REACH will apply to approximately 2,000 chemical substances imported into or manufactured in Korea in volumes of 100 tons or more annually or with a highly hazardous nature, which are already listed on the Korea Existing Chemicals List. It will require Korean manufacturers and importers of such chemical products to submit information on the toxicity data and their potential exposure. More specifically, this overhaul of Korean chemicals management legislation will be implemented in several steps by 2012: Step 1 – Impose toxicity examination of existing chemicals-Implementation of Korea REACH; Step 2 – improve/implement the survey on amounts (volumes of highly hazardous chemicals) in circulation and for inclusion in a published Toxic Release Inventory ('TRI'), and identify companies that will be subject to the TRI; Step 3 – improve the designation of restricted and prohibited chemicals for purposes adding new such chemicals to the survey and TRI in the future; and Step 4 – expand test data requirements for toxicity examination for new chemical notifications. See *MOE's Plans for Improvement of Chemical Management*, Kim & Chang Chemical News & Updates (May 12, 2008) at: http://www.aem.org/AllDocuments/AEM/SRT/SRTTopics/REACH_2009-05-12_KoreaImplementation.pdf .

D. *China Regulations*

- **China RoHS** - Joint Ministerial Decree No. 39: Management Measures for Controlling Pollution by Electronic Information Products, referred to as the China RoHS, was issued February 28, 2006, and based on the Law on the Promotion of Clean Production, which took effect on January 1, 2003. It is comprised of two components/phases: Phase 1 - a labeling mandate pursuant to which all electronic information products (EIP) must be marked with the appropriate pollution control logo and indicate the environmental protection use period (effective, March 1, 2007); and Phase 2 - restrictions imposed on products listed in the Catalog for Priority Pollution Control, which may not contain

RoHS substances and must pass China's compulsory product certification (CCC). Phase 2 has not taken effect because the catalog has not been published.

"'Electronic Information Products (EIP)' referred to in Phase 1 are defined as products that use 'electronic information technology', such as: electronic radar products (except military radar), electronic communications products (transmission, receiver, switching), broadcast and television equipment (transmission, receiver, production), computer products (large-frame, network, PC, media), home electronic products (TV, video & stereo equipment), electronic measuring instruments, specialized electronic products (industry manufacturing equipment), electronic applications (medical equipment, games, microwave oven), electronic components and parts, and electronic materials…

Thus, the scope of the China RoHS is generally broader than that of the EU RoHS. For example, the EU RoHS targets consumer products, not commercial or industrial equipment. The EU RoHS does not apply to equipment rated over 1000 volts AC or 1500 volts DC. And, the EU RoHS specifically excludes large-scale stationary industrial tools, medical devices and monitoring & control instruments. Unlike the EU RoHS, the China RoHS applies to medical equipment, measuring instruments, radar, communications transmission and switch equipment, and manufacturing equipment for electronic products. The China RoHS also covers both batteries and packaging materials for electronic products, whereas the EU RoHS has separate battery and packaging directives. See *What is China RoHS Phase 1?*, RSJ Technical Consulting at: http://www.rsjtechnical.com/WhatisChinaRoHS.htm .

- "On July 16, 2010, the Chinese government's Ministry of Industry and Information Technology (MIIT) issued a proposed update to China's RoHS - the 'Draft Measures for the Pollution Control of Electrical and Electronic Product (EEP)', for public consultation until August 19, 2010…The proposed updates would change the coverage of products by modifying the definition *from* 'Electronic Information Product' *to* 'Electrical and Electronic Product'…'Electrical and Electronic Product' is defined…as 'equipment or its accessories which work with a voltage rating not exceeding 1500 volts for direct current and 1,000 volts for alternating current'…If…adopted…the new definition would immediately subject all EEP to China RoHS because no product categories would be defined. The current China RoHS identifies covered products in a Catalogue. The new definition of EEP is an even broader coverage of regulated products than that which is currently discussed in the EU Recast proposal." *See* Michael Kirschner, *China RoHS Update Up for Public Consultation until August 19*, Connections IPC Blog (July 27, 2010) at: http://blog.ipc.org/2010/07/26/china-rohs-update-up-for-public-consultation-until-august-19/.

- **China REACH** – China, intending to protect its own workers, published proposals for its equivalent to the EU REACH regulations during May 2009. While the proposed regulation's aim of controlling the manufacture, import and use of chemicals is similar to the EU REACH regulations, this proposal included very few obligations affecting substances in 'articles' (i.e., as 'fabricated products'). Yet, it is "clear that some of the most hazardous substances could eventually be phased out in China and this could affect the availability of some process materials and possibly also fabricated products." On a related note, during January 2010, "the Chinese Government published and adopted amended legislation", effective October 15, 2010, which does not apply to articles. Rather, it applies mainly to chemicals and mixtures of chemicals and includes requirements for new chemicals that are released from articles during normal use. Like the EU REACH, this Chinese law requires that intentionally released chemicals (if greater than one tonne) should be registered. The main focus of the China REACH obligations is on manufacturers of substances in China and importers of substances into China. It also clearly refers to the GHS (Globally Harmonised System) labelling system. *See* Gary Nevison, *China REACH Regulations Reduce the Temptation for Companies to Move Manufacturing out of Europe*, Electronics World (June 22, 2010) at: http://www.electronicsworld.co.uk/index.php/template/warp-slick-template-framework/2883-china-reach-regulations-reduce-the-temptation-for-companies-to-move-manufacturing-out-of-europe ; Gary Nevison, Chinese Chemicals legislation - "China REACH", (February and July 2010) at: http://www.element-14.com/community/docs/DOC-21086 .

III. Government Procurement Requirements

A. United States - Integrating Green Purchasing Into Your Environmental Management System (EMS) April 2005 (EPA 742-R-05-001 (United States Federal Government)

- Environmental standards and guidelines developed by federal and independent standards-setting organizations including:
    - Design for the Environment (DfE) Program for lower hazard products (EPA)
    - Comprehensive Procurement Guidelines for recycled-content products (EPA)
    - Biopreferred Program for biobased products (US Department of Agriculture)
    - ENERGY STAR® and Federal Energy Management Program (FEMP) for energy efficient products (Department of Energy & EPA)
    - WaterSense for water efficient products (EPA)
    - ASTM, ANSI, Green Seal, EcoLogo, Scientific Certification Systems, MBDC Cradle to Cradle and other independent and non-governmental "green" product certification programs.

  See *Database of Environmental Information for Products and Services*, at: www.epa.gov/epp/database.htm and http://yosemite1.epa.gov/oppt/eppstand2.nsf .

- Presidential Executive Order (EO) 13148: Greening the Government Through Leadership in Environmental Management -
    - Mandates that all appropriate Federal facilities implement Environmental Management Systems (EMS) by December, 2005;

- Presidential Executive Order (EO) 13514: Federal Leadership in Environmental, Energy and Economic Performance (Oct. 2009)
    - Each federal agency's goal is to "to ensure that 95 percent of new contract actions including task and delivery orders, for products and services with the exception of acquisition of weapon systems, are energy- efficient (Energy Star or Federal Energy Management Program (FEMP) designated), water-efficient, biobased, environmentally preferable (e.g., Electronic Product Environmental Assessment Tool (EPEAT) certified), non-ozone depleting, contain recycled content, or are non-toxic or less toxic alternatives, where such products and services meet agency performance requirements".

B. European Union

IV. Voluntary Industry-Based International Standards Development Organizations

A. *International Organization for Standardization (ISO)*

- ISO 9000 – management system;
- ISO 14000 – environmental management system;
- ISO 26000 – social responsibility system
- ISO, etc.

B. *International Electro technical Commission (IEC)*

C. *International Telecommunications Union (ITU)*

D. *EU Eco-Management and Audit Scheme (EMAS)* – (actually a regional EU regulation on the voluntary participation by organisations in a Community eco-management and audit scheme - REGULATION (EC) No 1221/2009);

E. *Informal ICT Standards Consortia - World Wide Web Consortium (W3C), etc.*

V. Industries Incorporating Voluntary Standards into Supply Chain Contracts

A. *Supply Chain Management*

"*[S]upply chain management encompasses the planning and management of all activities involved in sourcing and procurement, conversion, and all logistics management activities. Importantly, it also includes coordination and collaboration with channel partners, which can be suppliers, intermediaries, third-party service providers, and customers. In essence, supply chain management integrates supply and demand management within and across companies*."

See *Council of Supply Chain Management Professionals* (September 2007) description reproduced in Tsan-Ming Choi, *Mean-Variance Analysis of Supply Chain Contracts*, European Journal of Operational Research, Vol.184, Issue 1, (Jan. 2008), pp. 356-376 at: http://www.intechweb.org/downloadpdf.php?id=736 ; http://www.sciencedirect.com/science?_ob=ArticleURL&_udi=B6VCT-4MR1P4M-5&_user=10&_coverDate=01/01/2008&_rdoc=1&_fmt=high&_orig=search&_sort=d&_docanchor=&view=c&_searchStrId=1414577720&_rerunOrigin=scholar.google&_acct=C000050221&_version=1&_urlVersion=0&_userid=10&md5=5bb47ad99abf6dc2c1f80f153a7da18a .

B. *Supply Chain Contracts*

"Supply chain contracts represent the 'rules of engagement' for how partners will share the benefits and the risks from uncertain supply or demand…In summary, the sourcing of supply chain functions remains ideally described as an arrangement of cooperative inter-firm relationships based on mutual commitment and trust between buyers and suppliers (Johnston et al., 2004). *See* Tim Coltman, Kathrine Bru, Nidthida Perm-Ajchariyawong, Timothy M. Devinney and Gabriel R.G. Benito, *Supply Chain Contract Evolution*, European Journal Vol. 27, Issue 6, (Dec. 2009), pp. 388-401, at: http://www2.agsm.edu.au/agsm/web.nsf/AttachmentsByTitle/TD_NSB/$FILE/NSB.pdf ; http://www.sciencedirect.com/science?_ob=ArticleURL&_udi=B6V9T-4VM7YH7-1&_user=10&_coverDate=12/31/2009&_rdoc=1&_fmt=high&_orig=search&_sort=d&_docanchor=&view=c&_searchStrId=1414587646&_rerunOrigin=scholar.google&_acct=C000050221&_version=1&_urlVersion=0&_userid=10&md5=b9082353bccd81e7de291779d2451b44 .

"Increasing demands are being placed on suppliers to assure that their products are safe, reliable, and do not have adverse effects on the health and the safety of users or on the environment. These demands may come in the form of contract requirements imposed by customers, or as mandatory government regulations. *The supplier is faced with the task of ensuring that the product conforms to all imposed requirements.*" See Robert L. Gladhill, *CONFORMITY ASSESSMENT What is it, Why do we need it?*, ASTM Standardization News (Aug.1996) pp. 30-33, at: http://trace.wisc.edu/docs/taacmtg_sep96/gladhill.txt.

C. *Responsible Sourcing*

"Responsible sourcing/ supply chain responsibility, is a voluntary commitment by companies to take into account social and environmental considerations when managing their relationships with suppliers. Companies can take basic steps to influence and monitor social and environmental performance in their global supply chains. When choosing a supplier, in addition

to making a final determination on cost, companies often need to evaluate a range of supply chain issues: product quality and safety, continuity of supply and speed of delivery, and intellectual property protection. Criteria such as working conditions, environmental practices, safety standards, and human rights policies should also be factored into the selection process. When contracting with a supplier, companies should make it known that they expect their business partners to comply with all national laws and regulations, including labour and environmental laws, and as appropriate, to take into account principles from relevant international instruments, *which may sometimes go beyond local legislation*." For example:

- International Labor Organization (ILO) Declaration on Fundamental Principles and Rights at Work & other ILO conventions;
- UN Universal Declaration of Human Rights;
- UN Global Compact and its 10 principles' covering human rights, labour standards, the environment, and anti-corruption;
- Company supplier code of conduct benchmarked to industry-wide supplier codes of conduct. For example:

    - Business Social Compliance Initiative – See *BSCI – Who We Are*, at: http://www.bsci-eu.org/index.php?id=2008 and *BSCI – What We Do*, at: http://www.bsci-eu.org/index.php?id=2014 ;

    - Electronics Industry Citizenship Coalition – See *About EICC*, at: http://www.eicc.info/ABOUT.htm and *EICC Code of Conduct*, at: http://www.eicc.info/EICC%20CODE.htm;

    - International Council of Toy Industries CARE Foundation – See *Welcome to the ICTI CARE (Monitoring) Process*, at: http://www.icti-care.org/ and http://www.icti-care.org/process/monitoring-process.html;

    - Responsible Care Initiative – Chemicals Industry – See *Responsible Care – What We Do*, at: http://www.responsiblecare.org/page.asp?p=6407&l=1 and *Responsible Care Fundamental Features*, at: http://www.responsiblecare.org/pics/pdfs/ResponsibleCareFundamentalFeatures.pdf ;

    - Pharmaceutical Supply Chain Initiative (PSCI) – See *About the Pharmaceutical Supply Chain Group*, at: http://pharmaceuticalsupplychain.org/about/ and *The Pharmaceutical Industry Principles for Responsible Supply Chain Management: Implementation Guide*, at: http://pharmaceuticalsupplychain.org/principles/implementation_guide ;

    - Worldwide Responsible Accredited Production - Apparel and Footwear Industries – See *WRAP – About Us*, at: http://www.wrapcompliance.org/en/about-us and

WRAP 12 PRINCIPLES, at: http://www.wrapcompliance.org/en/wrap-12-principles ;

- Social Accountability Accreditation Services (SAAS) - SA8000 – See *About SAAS*, at: http://www.saasaccreditation.org/about.htm , and *SA8000 Standard*, at: http://www.saasaccreditation.org/certSA8000.htm (SAAS-accredited independent certification bodies certify facilities that conform to the requirements of SA8000);

- Fair Labour Association – (protecting workers' rights) – See *FLA – About Us*, at: http://www.fairlabor.org/aboutus.html;

- The Ethical Trading Initiative – (promotes implementation of corporate codes of practice covering supply chain working conditions) – *See About ETI*, at: http://www.ethicaltrade.org/about-eti .

- U.S. Exporters should be aware that, before being able to enter into supply chain relationships with prospective foreign customers, such parties are likely to:

  - Examine social and environmental legislation in the countries of production of prospective suppliers and the level of enforcement in these countries to assess production risks;

  - Evaluate whether prospective suppliers qualify for independent certification of conformity with recognized social and environmental standards;

  - Require compliance with all applicable laws as a minimum standard;

  - Establish a desired level of performance and use a supplier code of conduct as a benchmark for compliance and incorporate supplier requirements into commercial contracts; *and*

  - Carry out assessments of suppliers' facilities and practices, including through independent monitoring where appropriate, or by organizing onsite visits and worker interviews.

  See *ICC guide to Responsible Sourcing - Integrating Social and Environmental Considerations into the Supply Chain*, International Chamber of Commerce Commission on Business in Society © 2008 at: http://www.iccwbo.org/uploadedFiles/ICC/policy/business_in_society/Statements/ResponsibleSourcing%20Brochure%20final.pdf .

VI. Multinational Companies Incorporating Regulatory and Voluntary Standards into Global Supply Chain Contracts

Before entering into contractual relations with prospective multinational customers/purchasers U.S. exporters should consider the following examples of company supply chain standards and conformity assessment requirements:

A. *Nokia Supplier Requirements; EU REACH Regulation*

- Provides each of its suppliers with information to ensure they are aware of the REACH regulations, understand the requirements and are taking responsibility for compliance to ensure uninterrupted supply;

- Focuses primarily on those suppliers *with whom the company contracts* and works directly. Company suppliers "are required to meet Nokia Supplier Requirements and product environmental requirements that define expectations for company suppliers, the components, parts and services they supply. Nokia Supplier Requirements request that our suppliers in turn set environmental, labor and health & safety requirements, and monitor the performance of their suppliers";

    - "Company developed a comprehensive set of global Nokia Supplier Requirements (NSR), which include specified environmental and social requirements. These requirements are based on international standards ISO 14001, SA 8000, OHSAS18001, PCMM and ILO, and UN conventions";

- "If concerns arise regarding the performance of 2nd/3rd tier suppliers, Nokia works deeper down the supply chain to investigate and address any concerns";

- Company "also developed environmental requirements for the products, components and parts that it sources. New suppliers (like our existing suppliers) must commit to meeting our requirements (e.g. NSR and environmental product requirements) *as part of the contractual agreement*."

See *Nokia Sourcing Materials*, at: http://www.nokia.com/corporate-responsibility/supply-chain/substance-management and *Nokia Supplier Requirements*, at: http://www.nokia.com/corporate-responsibility/supply-chain/substance-management .

B. *European Aeronautic Defence and Space Company N.V. (EADS) Supplier Management*

- EADS' "Procurement Marketing and Global Sourcing aim to identify the best potential suppliers worldwide and to evaluate them with regard to their capabilities and their certifications";

- "The EADS Supplier Evaluation and Development process guarantees that suppliers' performances are regularly evaluated. Suppliers can expect that the same process and the

same criteria are applied by all Business Units: Commercial, Logistics, Quality, Technical and Customer Support...Each EADS Division and BU has its own sourcing function";

- "Procurement Policies of EADS Business Units address all typical business risks, including risks attached to CSR, and suggest how they should be dealt with in EADS' contractual agreements";

- "Most of EADS' suppliers are currently located in the E.U. (77%) and North America (21%), regions in which social, economical and environmental practices are well regulated by applicable norms and laws. *EADS Sourcing contractual terms* request that these suppliers shall comply at any time with laws and regulations on economical, environmental and social standards and anticipate or at least make their best endeavour to anticipate forthcoming changes in these standards. To reinforce supply chain compliance to EADS CSR (Corporate Social Responsibility) related requirements, *EADS tier 1 suppliers are contractually bound to flow-down these requirements to tier 2 suppliers*."

    - "EADS is on one side engaged in a process for *embodying additional CSR requirements into procurement contracts* and on the other side EADS is organising supplier CSR performance measurement."

- "Sourcing Contractual terms related to CSR":

    - "EADS Sourcing Risk and Opportunities Management ("ROM") recommends contractual guidelines for the key contractual chapters. These guidelines are published in the EADS Sourcing Information Tool which *explains the principles for drafting contracts, disclaims the typical contractual clauses* and gives practical comments for the use by the buyer. *For each domain, the requirements are contractually cascaded on to sub-tier suppliers*;

    - "For example, regarding environmental responsibility, principles for drafting contracts state that: '*The purchase contract should provide that the supplier shall comply with all applicable laws, regulations, etc. as well as all commitment to which EADS has subscribed* (e.g., Global Compact initiative) and end-customer requirements, in particular: (1) Suppliers are asked to support a precautionary approach to environmental challenges; (2) Undertake initiatives to promote greater environmental responsibility; and (3) Encourage the development and diffusion of environmentally friendly technology.' The recommendation to the buyer also states that EADS encourages suppliers to implement an environmental management system complying with international standards such as ISO 14000 or EMAS."

    - "In terms of Compliance with EADS Ethical commitments, it is recommended that the contract includes EADS key engagements such as the support, respect and

protection of international human rights within the supplier's sphere of influence; the respect of the freedom of association and the effective recognition of the right to collective bargaining; the elimination of all forms of forced and compulsory labour; the quality of working conditions such as but not limited to, appropriate level of remuneration, and protection of health and safety of the employees";

- Within the "EADS Astrium Business Unit, [t]he CSR requirements are now considered in the Supplier pre-selection process as part of the basic Supplier requirements which are prepared in order to ensure in particular:
  - Compliance to EADS code of Ethics and CSR policies; and
  - Awareness and demonstration of compliance with applicable statutory and regulatory requirements: WEEE, RoHS, CE Marking, etc."

See *Supplier Management: Fostering a Mutually Beneficial Relationship with EADS' Suppliers*, EADS Annual Report and Registration Document 2006, available at: http://www.reports.eads.com/2006/en/book3/3/4/3/print.html (cache).

C. *Vodafone Code of Ethical Purchasing - Protecting Reputational Risk*

- "Ensuring [that] companies in the supply chain comply with labor and environmental standards is vital to managing reputational risk. Negative publicity has become one of the major risks to brand reputation…Managing this risk has pushed corporate responsibility (CR) to the top of the agenda for many corporations";
- "In July 2003, the Vodafone Group Policy Committee approved the company's Code of Ethical Purchasing (CEP). The code was developed in consultation with employees, suppliers, investors and NGOs, including Morley Fund Management, ISIS Asset Management, Fauna and Flora International, Save the Children Fund and WWF" (See Code of Ethical Purchasing, at: http://vodafone.com/start/responsibility/supply_chain/code_of_ethical_purchasing.html);
  - "The CEP is based on Vodafone's corporate values as well as international standards such as the Universal Declaration of Human Rights and the International Labor Organization (ILO) conventions on labor standards. It aims to ensure safe and fair working conditions and responsible management of environmental and social issues in the supply chain";
  - "At the end of 2003 and the beginning of 2004, *Vodafone began putting the CEP in contracts with key global suppliers*, including Panasonic Mobile. Vodafone also set a public goal to measure CEP implementation with three major suppliers,

and the joint pilot assessment with Panasonic Mobile was a way of fulfilling that goal";

- During 2004-2005, Vodafone set the following goals:
  - "Ensuring its top 25 global suppliers complete Vodafone's self-assessment questionnaire to determine compliance with the CEP";
  - "Completing assessments of five of the top 25 global suppliers against the CEP, including one or more facility audits";
  - "Ensuring the top three suppliers to each operating company complete Vodafone's self-assessment questionnaire to determine compliance with the CEP, an initial element of the assessment process";
  - *Incorporating the CEP into the contracts of all of Vodafone's top 25 global suppliers;*

See Saul Jamieson, *Cooperating on a Supply Chain Audit at Vodafone and Panasonic Mobile - Checking Compliance with Ethical Standards at a Mobile Telephone Factory in the Philippines*, Melcrum Publishing at: http://www.melcrum.com/articles/supply_chain_at_Vodafone_and_Panasonic.sht ml

D. *Glaxo Smith Kline – Responsible Supply Chain*

- "The company's approach to ensuring high EHS and human rights standards among its global suppliers includes":
  - "Pre-audit assessments of potential suppliers to gather information and to help evaluation";
  - "*Inclusion of a human rights clause in supplier contracts and full environment, health and safety (EHS) requirements in contracts for critical suppliers*";
  - "Review of EHS and human rights in routine supplier engagements";
  - "EHS audits of potential and existing suppliers";
  - "Agreed improvement programmes with suppliers";
  - "Regular progress monitoring and advice";
- Supplier contracts –

  - Company "*supplier contracts contain EHS requirements based on our global EHS standards and human rights clauses based on the International Labour Organization conventions and the UN's Universal Declaration of Human Rights. Companies must agree to our EHS and human rights requirements before they can be included as a supplier*";

- The company "focus[es] on 'critical suppliers' that represent approximately 30 per cent of our supplier spend, and are mostly based in Europe, North America and Asia. Critical suppliers include contract manufacturers and suppliers that are pivotal to company business. We consider the following factors when defining critical suppliers who may present a high risk to GSK:

  - Relevance to the supply of essential medicines;
  - Threats to continuity of supply;
  - The value of affected products to GSK;
  - Regulatory compliance and requirements;
  - Hazards associated with manufacturing processes and materials;
  - Environmental impacts.

  We develop long-term relationships with critical suppliers and conduct regular monitoring to support the uninterrupted supply of high quality materials and services to GSK."

- "The company trains all new procurement employees in our standards and requirements for EHS and human rights";

- "The company collaborates with other companies in the Pharmaceutical Supply Chain Initiative (PSCI)…[which] has developed the Principles for Responsible Supply Chain Management to provide guidance for suppliers on the standards that the pharmaceutical industry expects. These align closely with GSK's EHS and human rights standards."

- The company is "adding environmental sustainability topics to the questionnaires we use to assess potential new suppliers. In 2010 we will start to introduce sustainability requirements for existing critical suppliers and will use supplier review meetings to encourage these companies to improve their sustainability performance."

See *Responsibility and Our Supply Chain*, GSK Our Responsibility Report 2009, at: http://www.gsk.com/responsibility/supply-chain/responsibility-and-our-supply-chain.htm

E. *Newmont Mining Co.'s Supply Chain*

- Company "operations depend on our ability to acquire the right goods and services, at the right price, at the right time and in the right manner. We achieve this by using a global, managed category, total-cost approach to supply chain management, while ensuring safety and environmental compliance. It isn't enough to just get necessary goods to the operations; we must conduct these transactions in an environmentally and socially responsible manner."

- "To drive responsible and efficient purchasing, Newmont's supply chain group:

    - "*Enforces all aspects of social accountability standards (SA 9000) in our contracts with each supplier* to prohibit any use of child/convict/slave labor by any company with which Newmont does business";

    - "Requires and enforces all suppliers to abide by Partnering Against Corruption Initiative (PACI) terms in our contracts";

    - "Only does business with cyanide vendors that are signatories to the International Cyanide Code and are current on their audits";

    - "Newmont is currently voluntarily implementing stringent greenhouse gas programs and guidelines, including auditable inventory profiles prior to mandatory legislation";

    - "*Strictly enforces U.S. environmental standards globally and for vendors*";

    - "Ensure that all vendors are held to the highest standard *through Newmont's influence and written contract*. Our vendors are contractually bound to continue to act in an environmentally sensitive and socially acceptable manner";

    - Company "standards also require that all major and many minor vendors participate in human rights screening. We estimate that currently 75 to 80 percent of contracts comply with this standard."

  See *Newmont Mining Co. – Our Supply Chain*, at: http://www.newmont.com/about/supply .

F. *Hewlett Packard (HP) Social and Environmental Policies*

- "Company Supply Chain Social and Environmental Responsibility Policy is available on HP web site at: http://www.hp.com/hpinfo/globalcitizenship/environment/pdf/suppolicy.pdf";

- "Company publicly endorsed and signed the UN Secretary General's Global Compact";

- "Company uses the Global Reporting Initiative (GRI) reporting framework";

- "Company was the first electronics company to publish a Social and Environmental Responsibility Supplier Code of Conduct";

- "In 2004, company helped lead the development of the Electronic Industry Code of Conduct (EICC), the standard it now applies";

    - "The EICC promotes industry standards for socially responsible business practices across the global supply chain;

    - "The EICC has replaced HP's Supplier Code of Conduct";

    - "All suppliers involved in manufacturing HP's products must meet or exceed the Electronic Industry Code of Conduct standards";

- "Company is an active member of CSR Europe and play a lead role in many CSR forums";

- "We expect our product material suppliers to act as responsible corporate citizens and take a positive, proactive stance regarding social and environmental issues…Suppliers must comply with HP's requirements specified in the Electronic Industry Code of Conduct and HP's General Specification for the Environment (GSE)".

See *HP - Supply Chain SER (Supplier Social and Environmental Responsibility) Frequently Asked Questions*, at: http://www.hp.com/hpinfo/globalcitizenship/society/supplychain/scserfaqs.html .

VII. Conclusion