

Safeguarding corporate social responsibility (CSR) in global supply chains: how codes of conduct are managed in buyer-supplier relationships

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- *In the wake of globalization, companies are becoming increasingly aware of the social and environmental aspects of international production. Companies of today not only have to be profitable, but they also have to be good corporate citizens. In response to the increasing societal pressure, many companies adopt the concept of corporate social responsibility (CSR) by introducing codes of conduct that are expected to ensure socially responsible business practises throughout the chain—from supplier of raw materials to final end-users.*
- *However, there are several challenges to the management and control of codes of conduct in global supply chains. Active commitment is a precondition for the successful implementation of the codes, but the incentive to comply with the codes does not necessarily extend to all the actors in the chain. Moreover, it is difficult to enforce codes of conduct in global supply chains, because the involved companies are separated geographically, economically, legally, culturally and politically. In consequence, introducing codes of conduct in global supply chains raises a series of agency problems that may result in non-compliance.*
- *Realizing that non-compliance can have severe consequences for the initiator (due to consumer sanctions, negative press, capital loss, government interventions, damaged brand etc.), the article analyses how the interests of the actors in the supply chain can be aligned with the terms of the codes. IKEA is used as a 'best case' example to illustrate how codes of conduct can be effectively managed in the supply chain.*

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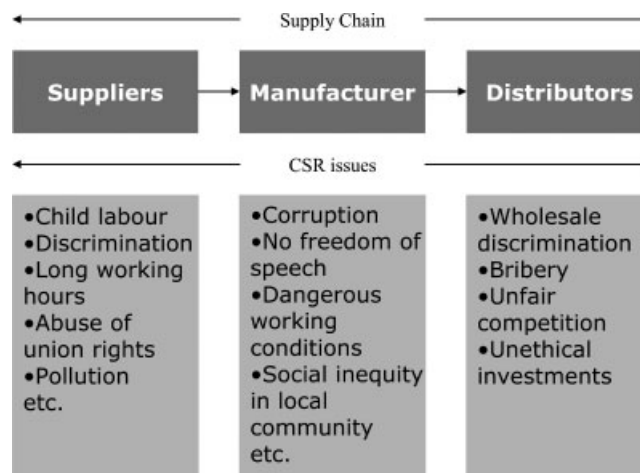


Figure 1. Examples of CSR issues in supply chains (Neergaard and Pedersen 2005, p. 103). Inspired by WBCSD (2003).

Introduction: CSR in global supply chains

Doing the right thing in business is no longer just a matter of making profit. The ethics of business activities are becoming increasingly important, and more and more companies are evaluated on their ability to meet not only the customers' needs but also the various needs of employees, NGOs, the local community representatives and other interest groups. In response to this development, companies are increasingly embracing the discourse of CSR, and a wide range of international organizations, business associations and standardisation organizations have recently introduced management standards, labelling schemes and reporting systems, which all address the social and environmental aspects of production (Utting, 2000, p.1; Kapstein, 2001, p. 114; Kolk and van Tulder, 2003, p. 267).

Moreover, a large number of especially multinational corporations (MNCs) have introduced Codes of Conducts, that is a set of written principles, guidelines or standards, which are intended to improve the company's social and environmental performance. Realizing that CSR issues arise throughout the supply chain (see **Figure 1**) and that companies are increasingly held responsible for the conditions under which their products are being produced, these codes often go well beyond the

boundaries of the individual organization and include social and environmental requirements for suppliers (cf. Roberts, 2003, p. 163; Jenkins, 2005, p. 527).¹

When the success of CSR depends on the actions of all parties in the supply chain, the governance of these inter-organizational relationships are of crucial importance. Failure to manage and control the social and environmental impact of the supply chain will increase the risk of non-compliance, which in turn may damage the reputation of the company that developed the code (the initiator). One thing is to be socially irresponsible; another is to be a socially irresponsible liar. In other words, the initiator of a code has a strong incentive to ensure that the other companies in the supply chain comply with the code.

So far, much research has addressed the question of whether CSR initiatives are reliable from the perspective of the various interest groups in society (e.g. unions, NGOs, government, customers). Much less has been done in order to investigate how companies safeguard CSR in global supply chains. Realizing the complexity and difficulties in managing external relationships with independent companies operating in different geographical,

¹According to the World Bank (2003, p. 2), there is an estimate of approximately 1000 of these codes in existence today World Bank (2003A, p. 2)..

social and political settings, the question is how a company can be certain that the suppliers fulfil their obligations stated in the code.

Theoretical perspective

Based on a simple buyer (principal)—supplier (agent) relationship, the article will try to answer this question by presenting some of the safeguards/protective mechanisms on which a company may rely when planning and implementing Codes of Conduct in global supply chains. The presentation will be based primarily on agency theory, which is useful in the analysis of most cooperative efforts, where it is difficult for a principal to monitor the work of the agent. Moreover, a number of related theories (most notably transaction cost theory) and alternative perspectives (most notably network theory) will serve as discussion partners in the analysis.

Agency theory assumes that individuals are self-interested creatures and addresses the problem of opportunism, that is, self-interest seeking with guile (Dees, 1992, p. 29; Koch, 1995, p. 3; O'Donnell, 2000, p. 526). With regard to the latter, it is not expected that all individuals are opportunistic, but that some are, and that it is difficult and costly to separate the opportunistic actors from the non-opportunistic ones (Williamson and Ouchi, 1981, p. 351). In order to avoid opportunism, it is necessary to provide the agent with incentives to act in accordance with the principal's interests (Dees, 1992, p. 25; Petersen, 1993, p. 277; Koch, 1995, p. 13). In short, this can be done either by monitoring behaviour or rewarding outcomes (Eisenhardt, 1989, p. 61; Petersen, 1993, p. 281; O'Donnell, 2000, p. 526). Monitoring can be seen as a mechanism used by the principal to obtain information about the actions of the agent, whereas rewards are outcome-based, financial incentives (cf. O'Donnell, 2000, p. 526). However, both alternatives are associated with costs, which depend on the characteristics of the activity (the complexity of the assignment, the ability to monitor the agents, the correspondence

between outcome and the agents' behaviour etc.).²

Agency problems and codes of conduct

It is generally acknowledged that opportunism poses a threat in inter-firm relationships, and one case in point is the planning and implementation of Codes of Conduct in global supply chains (see e.g. O'Donnell, 2000, p. 526; Das and Rahmann, 2000, p. 89). To be more specific, opportunism in relation to Codes of Conduct and other CSR standards becomes relevant due to the fact that these initiatives can be costly and time consuming (See e.g. Walley and Whitehead, 1994, p. 46; Kolk, 2000, p. 118–119; Sinding, 2000, p. 86; Utting, 2000, p. 26; Kapstein, 2001, p. 115). In consequence, suppliers might have an economic incentive to reduce social and environmental standards in order to achieve financial gains. Moreover, the potential benefits from introducing Codes of Conduct might be unevenly distributed among the companies in the supply chain. For instance, goodwill from being socially responsible is often associated with a brand, which only one of the companies in the chain holds. This company will receive the full benefits from introducing a Code of Conduct. The rest of the companies in the chain will have to share the indirect benefits, for example from new deliveries. If these companies furthermore have to bear the costs of implementing CSR initiatives, there is a potential conflict of interest between the companies in the chain. This increases the risk of opportunistic actions.

It would be easy to deal with this opportunism if it were possible to formulate an enforceable contract, which included all contingencies (Milgrom and Roberts, 1992, p. 127; Greve, 2000, 155). However, most contracts

²More formally, agency costs can be defined as: "(...) the costs of structuring, monitoring and bonding a set of contracts among agents with conflicting interests. Agency costs also include the value of output lost because the costs of full enforcement of contracts exceed the benefits" (Fama and Jensen, 1986, p. 279). See also Jensen and Meckling (1976).

are incomplete and this applies to Codes of Conduct as well. As noted by Utting (2000, p. 12–13): ‘Codes very often remain at the level of lofty principles and well-intentioned policy statements that are not effectively implemented (...)’. In line with Utting, Sethi (2002) also criticizes Codes of Conduct for typically being presented as public statements of lofty intent and purpose without a specific content. In consequence, it becomes difficult to verify whether a supplier has actually complied with the Code of Conduct. Moreover, Klein argues that ‘codes of conduct are awfully slippery’ (2000, p. 430). This statement is based on the argument that the codes cannot be enforced in the same way as legal requirements, and that they are not drafted in response to the needs of the employees of the companies they are directed towards. Historically, Codes of Conduct have also been characterized by a remarkable lack of efficient monitoring systems. Only a minority of firms with Codes of Conduct actually mention monitoring in relation to the implementation, and the majority of these use internal systems (Kolk *et al.*, 1999, p. 169; Kolk and van Tulder, 2001, p. 274; OECD, 2000, p. 31).

Safeguards/protective mechanisms

The potential conflict of interest between the companies in the supply chains and the incomplete nature of Codes of Conduct makes it relevant to discuss how an initiator of a code can be ‘safeguarded’ from non-compliance on part of its suppliers. It is worth mentioning, however, that opportunism occurs in all relationships between individuals, and thus safeguarding is relevant in the understanding of all aspects of the social and economic life.

Safeguards, or protective mechanisms, are basically means to ensure that an agent fulfils his or her obligations according to the agreement (Koch, 1995, p. 8). Safeguarding includes elements of different theories, but the purpose of this article is neither to give a detailed presentation of the different positions, nor to engage in the dogmatic discussions between

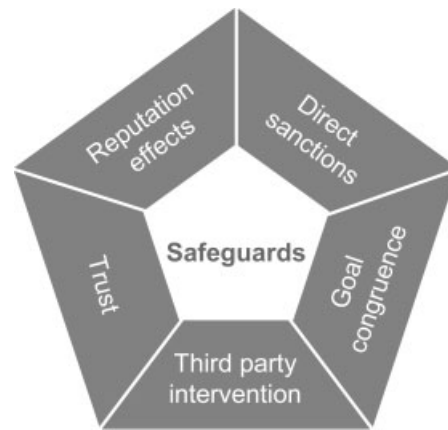


Figure 2. Safeguards/protective mechanisms. Source: Based on Koch (1995, 1997)

them. Instead, the article intends to discuss how safeguards can ensure compliance with Codes of Conduct in global supply chains.

The safeguards/protective mechanisms dealt with in this article are direct sanctions, goal congruence, third-party intervention, trust and reputation effects (see below).³ In the following sections, we will present each safeguard in turn and discuss how they are manifested in the Swedish home furnishing retail chain, IKEA.

Safeguarding mechanisms at IKEA⁴

IKEA is a Swedish home furnishing retail chain selling low-priced products, including furniture, accessories, bathrooms and kitchens. The company was founded in 1943 by Ingvar Kamprad. *IKEA* is short for *Ingvar Kamprad, Elmtaryd*—the farm he grew up at, and *Agunnaryd*—the village he grew up in. To begin with, IKEA sold pens, wallets, picture frames, table runners, watches, jewellery and nylon stockings at low prices. The first

³This classification is based on the work of Koch (1995, 1997). It is by no means stated that the classification is definitive. The different types of safeguards are inter-related, and depending on perspective and interest, some of them could probably be united or split up. However, it is argued here that the five safeguards give a fairly representative overview of some of the means, which are relevant for companies implementing Codes of Conduct in global supply chains.

⁴The analysis is based on written documentation and interviews with representatives of IKEA. Conducted in 2004.

furniture showroom opened in 1953 in Älmhult, Sweden, which is still the location of IKEA's headquarters. Two years later, IKEA began designing its own furniture, and in 1958, the first IKEA store opened in Älmhult. From the outset, the idea was to design furniture at low prices. After a while, the company also began to think in terms of designs suitable for flat packaging, which led to even further price reductions. Today, IKEA employs approximately 90 000 co-workers and operates in 44 countries. In the financial year 2004, sales totalled 14.8 billion euro.

IKEA's product range is produced by approximately 1300 suppliers according to product specifications developed by IKEA. Almost 2/3 of the suppliers are located in Europe and 1/3 in Asia. Only 3% of the suppliers are from North America. Purchasing is handled by 46 'trading service offices' divided into 16 regional 'trading areas'.

Recognizing that negative publicity about the environmental or social conditions of its suppliers might damage the IKEA name considerably, the company realized by the end of the 1990s that it needed to relate actively to the environmental and social conditions of its suppliers. Therefore, the company decided to develop a Code of Conduct aimed at all its suppliers worldwide. The code is labelled '*The IKEA Way on Purchasing Home Furnishing Products*'—in day-to-day operations referred to as 'IWAY', and it was introduced in year 2000. IWAY defines what the suppliers can expect from IKEA and what IKEA requires from its suppliers with regard to working conditions, child labour, environment and forestry management. IKEA requires from its suppliers to comply with national laws and regulations and with international conventions on the protection of the outside environment, working conditions and child labour. The suppliers are expected to abide by the most demanding of the requirements, whether it is the applicable legislation or IKEA's specific requirements. IWAY includes 19 different areas divided into more than 90 specific issues.

Direct sanctions

Contracts, complete or incomplete, are of little use, if it is impossible to enforce them. However, the description of monitoring and the consequences of non-compliance are often absent in Codes of Conduct (see e.g. Kolk *et al.*, 1999, p. 167–169). In consequence, it is rather unclear, what sanctions are open to a buyer, which discloses a supplier's non-compliance with a code.

The fastest and most ultimate sanction is to break off the relationship with the supplier in case of non-compliance. However, this exit strategy has certain limitations. Most importantly, the principal's ability to terminate an agreement depends on the bargaining power of each party in the relationships. Exit is only applicable as a safeguard, if it is a credible threat. Hence it follows that the threat of exit has little effect, if the supplier's products and services are of vital importance to the buyer (buyer-dependence). On the contrary, the supplier has a strong incentive to honour the terms of a Code of Conduct, if the future of the company depends on continuous co-operation with the buyer (supplier-dependence) (Helper, 1990, p. 5; Hill and Jones, 1992, p. 142; Buvik and Reve, 2002, p. 265).

The way direct sanctions work in IKEA is that each supplier is audited against the code by IKEA's own auditors. As the company has a strategy of engaging in long-term relationships with its suppliers, it does not break off relations due to non-compliance with IWAY requirements as long as the suppliers show a willingness to improve conditions. Instead, it requires that the suppliers prepare a written action plan detailing how the non-compliance issues will be rectified. The company requires that the suppliers carry out the corrective actions within a period of 24 months. If a supplier is not able to fulfil the IWAY requirements within this time frame, but shows a positive attitude towards implementation of IWAY, he is put on a 'risk register' and given additional time to fulfil the requirements. However, IKEA is willing to terminate the relationship with suppliers who do not show an interest in fulfilling all the IWAY requirements. And the company has in fact terminated

supplier relationships, either partly or entirely due to lack of IWAY fulfilment. Thus, since IWAY was introduced in 2000, a total of 354 supplier contracts have been terminated (Andersen, 2005, p. 141). Of these, 6% were terminated mainly due to non-compliance of IWAY issues, and 11% were terminated partly due to non-compliance of IWAY issues. IKEA's ability to use contract termination as a safeguarding mechanism should in large part be seen in the light of its size. Due to its large size, IKEA constitutes an important customer for many of its suppliers. The Regional Quality Manager puts it this way:

"When we place an order, we are not talking about 250 pieces only—we are talking about 25 to 50 containers. This factor alone has the effect that a supplier almost turns his factory upside down just to deliver to us".

As a result of their dependence on IKEA as a customer, many suppliers are often willing to go to great lengths to fulfil IKEA's IWAY requirements. They simply cannot afford to give the code a low priority, as this might imply a termination of the relationship with IKEA, which in turn could be very damaging to their business. We might therefore argue that the case of IKEA indicates a great deal of supplier-dependence.

In summary, direct sanctions can be a very efficient safeguard, if the buyer is the dominant partner in the business relationship (unless non-compliance is likely to go undetected, of course) (Koch, 1995, p. 14). If not, the buyer might envisage more subtle means, which will alleviate the fear of opportunism. Moving beyond the scope of institutional economics, buyer-supplier dialogue during the planning and implementation process can be an important element in this process (see next section).

Goal congruence

Implementation of Codes of Conduct requires some kind of motivation and commitment. In supply chains, however, it is not enough that the initiating company is dedicated to social

and environmental issues. The company must persuade the other organizations in the supply chain to act socially responsible too. In a buyer-supplier relationship, this might be difficult, if for example a supplier shows no interest in CSR or the buyer holds limited bargaining power against the supplier.

Opportunism is only likely to occur, if there is a conflict of interest between the principal and the agent. The basic idea of agency theory is therefore to give the agent incentives to act in accordance with the principal's interest (cf. Dees, 1992, p. 28; Milgrom and Roberts, 1992, p. 185–188; Koch, 1995, p. 13). Higher levels of goal congruence in relation to Codes of Conduct can be acquired in numerous ways: (1) the buyer can compensate the supplier for costs associated with code compliance. For instance, the buyer and supplier can make jointly investments in environmental friendly machinery; (2) the buyer can reward the supplier for complying with the code. As an example, the supplier can get an exclusive right to deliver products and services to the buyer; (3) the parties can undertake joint investments in transaction specific assets which will commit both of them to the relationship; (4) by referring to the strategic potentials of CSR, the buyer can convince the supplier that they will both be better off in the future, if they implement the code; (5) the buyer can involve the supplier in the planning and implementation of the Codes of Conduct, thereby stimulating commitment and goal congruence.

With regards to the latter, using non-economic incentives to increase commitment is normally outside the scope of standard agency theory. It is nonetheless worth noticing that if it is possible to create commitment to the Codes of Conduct, whatever the means, compliance is more likely to be accomplished. If the Codes of Conduct are implemented as a top-down approach, where the suppliers have little influence on the terms, it might be difficult to ensure commitment to the project. A bottom up/voice approach, where both the buyer and supplier are involved in whole process, might be an important element in a successful implementation of Codes of Conduct (cf.

Helper, 1990, p. 6; Schary and Skjøtt-Larsen, 2001, p. 183).⁵

IKEA puts great efforts into ensuring goal congruence between itself and its suppliers. The company makes use of several of the above-mentioned means. First of all, IKEA makes sure to emphasize up front to the suppliers that it does not require IWAY fulfilment just for its own sake, but that it is indeed important for the suppliers' employees as well as environmental surroundings. Secondly, the company lets the suppliers know that IWAY is a great opportunity for receiving assistance to build up some well-functioning environmental and social routines. The Regional Quality Manager explains:

"We tell the suppliers that 'we will give you all the time you need, we will provide you with all the help you need. And if it costs you money, we will discuss that as well'. They have nothing to lose, but everything to gain".

As indicated, IKEA provides its suppliers with technical as well as financial support. To be able to provide technical support, the company trains its employees to follow-up on and support the implementation of the Code of Conduct requirements at the suppliers. Of particular importance in this process are the efforts to change the mind-sets of the suppliers, particularly in developing countries, and hence improve their knowledge and understanding of Code of Conduct-related issues. With regard to financial support, IKEA is willing to support the implementation of capital-intensive investments such as a wastewater treatment plant. Such support will normally be in the form of a loan, which the supplier will pay back, for example through deliveries to IKEA.

⁵However, even though the voice strategy is attractive to many academics, because it seems more constructive than the take-it-or-leave-it exit strategy, voice is not a panacea, which can be applied to all business relationships. The voice strategy requires information, communication and coordination between the buyer and the supplier, which will inevitably increase the transaction costs of the cooperation. These additional costs have to be compared with the benefits deriving from increased commitment and goal congruence (Helper, 1990, p. 10).

In conclusion, creating goal congruence is one of the main tasks in establishing efficient safeguards, which prevent the buyer against non-compliance. Especially in global supply chains, where monitoring is complicated and costly.⁶

Third-party intervention

Even though the principal believes that the agent has violated the contract, the conflict resolution is often in the hands of, for example, courts and arbitrators. The normal legal system is probably one of the most important protective mechanisms in this regard.⁷ However, there are a number of limitations to the legal system's ability to ensure compliance with Codes of Conduct in global supply chains. For instance, it is difficult for the legal system to impose sanctions on agents, unless they fail to comply with existing laws. Moreover, many Codes of Conduct include issues that are beyond the legal requirements, and in consequence non-compliance with codes does not necessarily mean non-compliance with the national laws. Last but not least, enforcement of codes is difficult in countries with a weak institutional structure. This is especially relevant to buyers, which engage in global supply chains involving suppliers in developing countries.

Even if the legal system were able to settle conflicts between buyers and suppliers, the system will still face difficulties in determining,

⁶However, it is worth noticing that time changes and so does the level of goal congruence between the buyer and supplier. As Koch (1995, p. 13) notes: '[c]hanges, unexpected or expected, originating "outside" the transactional relationship may change the situation to a considerable degree as well. In this case, low ex ante goal incongruence may well turn into high ex post goal incongruence'. Moreover, the societal expectations to the companies develop over time and these changes must be reflected in the codes. Therefore, goal congruence is not established once and for all. It requires continuous interrelation between the buyer and supplier and responsiveness to the changing societal demands.

⁷The normal legal system can be defined as: "(...) the regulatory body that can impose sanctions on the parties to a transaction in order to force them to fulfil their obligations" (Koch, 1995, p. 4).

whether the supplier has acted opportunistically or not. As mentioned earlier, Codes of Conduct are incomplete contracts. When the buyer and supplier are unable to account for all contingencies and formulate the Codes of Conduct in precise language, the resulting ambiguity of the agreement will leave room for different interpretations of the terms. In consequence, both the buyer and the third party might be unable to prove that the agent has not complied with the agreement (Milgrom and Roberts, 1992, p. 131-133).

Therefore, it is relevant to consider other third parties, which can safeguard the buyers from non-compliance, for example industry organizations, certification auditors, external consultants, NGOs or legal authorities (Diller, 1999, p. 118; Kolk *et al.*, 1999, p. 168). From a contractual point of view, it is of little relevance whether the buyer or a third party carries out the monitoring of the supplier. However, third parties might have special competences in evaluating code compliance, and most importantly the third parties will improve the reliability of the codes. Moreover, customers and other stakeholders might perceive third party monitoring as being more reliable and credible.⁸

As already mentioned, IKEA makes use of internal auditors for carrying out on-site audits at the suppliers. However, to ensure objectivity and credibility in the eyes of the stakeholders, the company also uses external auditing companies to conduct third-party verification audits of the suppliers. The Social and Environmental Manager for IKEA Group emphasizes the role of external audits by arguing that:

“If it’s internal, we need someone with other eyes to look into how we operate and manage it”.

⁸According to Kapstein (2001), the reliability of third-party monitoring can also be questioned. From a case study it was concluded that: “(. . .)[t]he auditors ignored hazardous chemical use, barriers to freedom of association and collective bargaining, violation of overtime and wage laws, and other infractions” (Kapstein, 2001, p. 116).

In fact, these compliance audits have revealed that some of IKEA’s own auditors have used too low judgement levels. The company has subsequently had to re-train some of the auditors to increase their competence level as well as re-audit suppliers. This indicates that in the case of IKEA, third-party intervention has in fact enhanced the credibility of IKEA’s monitoring work.

To sum up, third-party intervention might serve two purposes. Most importantly, third parties’ monitoring of code compliance serves as a protective mechanism, which can prevent violation of the codes. Moreover, third parties improve the credibility of the codes and signal commitment to the company’s stakeholders. In contrast to current practises in the business community, where most codes today are monitored internally, third parties should play a more prominent part in the monitoring of Codes of Conduct.

Trust

All theories have build-in assumptions, which are statements about the world, that are neither observable nor testable (Neuman, 1997, p. 41). With regards to the behavioural assumptions, trust versus opportunism has been one of the major controversies between network theory and the institutional economics (see e.g. Granovetter, 1985, p. 72; Ring and Ven, 1992, p. 492; Podolny and Page, 1998, p. 60-62). Both agency theory and transaction costs theory are inclined to see opportunism as a central behavioural assumption, whereas network theory favours the concept of trust (Williamson and Ouchi, 1981, p. 351; Petersen, 1993, p. 279; Foss and Koch, 1996, p. 190). However, both institutional economists and network theorists seem to agree that it is not essential that all economic agents are opportunists/trustworthy (Williamson and Ouchi, 1981, p. 351; Schary and Skjøtt-Larsen, 2001, p. 92). One might question then, whether opportunism/trust is a behavioural assumption or a variable, which the companies have to take into consideration when they engage in contractual relationships. Opportunism (lack of

trust) and trust (lack of opportunism) are interrelated and all co-operative activities will include aspects of both.

A high degree of trust between the buyer and supplier can be an efficient safeguard, which can reduce the costs from, for example, monitoring and performance evaluations.⁹ The question is how the buyer knows, which suppliers should be trusted. Agency theory seems to favour control in preference to trust, because it is difficult and costly to separate trustworthy agents from the opportunists. However, both agency theory and network theory nonetheless share the opinion that some kind of trust can develop over time in business relationships (Johanson and Mattson, 1987, p. 37; Eisenhardt, 1989, p. 62–63; Petersen, 1993, p. 286; Podolny and Page 1998, p. 60). In general, new buyer-supplier relationships are expected to be characterized by low levels of trust. Trust is something the company must accept in a world of incomplete contracts. However, as the relationship evolves over time, the partners might begin to feel a moral obligation towards the cooperation. Trust emerges between the parties, and in consequence, the governance can be more relaxed (Ring and Ven, 1992, p. 488–489; Child, 2000, p. 244–249; Buvik and Reve, 2002, p. 261). The basic argument seems to be that if a supplier could be trusted in past transactions, he or she is also likely to be trusted in future transactions. The cooperation can be seen as an ongoing screening process, where the principal and the agent learn about each other. In relation to Codes of Conduct, the buyers will often get a 'record' of experiences from working with the suppliers. Based on this information, the buyer will often have a fairly good idea about which suppliers should be monitored most carefully.

IKEA strives towards building up a high degree of trust between itself and the suppliers. This trust is in large part established as a result

of IKEA's choice of engaging in long-term relationships with a limited number of suppliers. Within the last few years, the company has changed its supplier strategy by going from 'trading to purchasing'. Whereas it previously engaged in short-term relationships with many smaller suppliers, where the focus was on buying articles, IKEA is today increasingly engaging in long-term relationships with fewer suppliers, where the focus is on buying capacities. Moreover, whereas IKEA previously *demand*ed a certain level of quality, service, price and environmental and social responsibility of its suppliers, the company is now *developing* these issues together with the suppliers (Andersen, 2005, p. 115). This new way of relating to the suppliers implies that both parties are committed to working hard to make the relationship work. Termination of supplier relationships is accordingly less frequent today, since both parties have typically invested much money and time in the relationship. Moreover, by virtue of the long-term relationships, frequent interaction takes place between IKEA's employees and the suppliers' employees. This has in turn laid the ground for the establishment of a fairly high degree of personal trust.

When looking specifically at the implementation of IWAY at the suppliers, IKEA seems to put much effort into making sure that its follow-up activities take place in a cooperative manner and hence do not have a resemblance to a 'police function'. This is so as IKEA spends much time explaining to and showing the suppliers how to improve their non-compliance issues. This could be seen in contrast to follow-up activities based almost solely on controlling whether the suppliers rectify these non-compliance issues. IKEA's way of approaching the follow-up activities signals to its suppliers that it has trust in their ability to implement IWAY. On the other hand, a stronger degree of control would probably make the suppliers believe that IKEA does not have much trust in their capabilities. In consequence, trust-based follow-up activities are likely to give the suppliers greater incentives to implement IWAY.

⁹In this article, trust is defined as: "(...) *the confidence of a person, group, or organization relating or transacting with another under conditions of some uncertainty that the other's actions will be beneficial rather than detrimental to it*" (Child, 1998, p. 243–244).

In summary, trust can be an efficient safeguard, especially in long-term relationships, where the buyer and supplier have accumulated a thorough knowledge about each other. (Diller, 1999, p. 109). It will be a waste of resources to monitor suppliers, which traditionally have been proactive in the implementation of social and environmental standards. In the planning and implementation of the codes, the buyer can use experiences from past transactions with suppliers to target the monitoring of suppliers.

Reputation effects

Related to trust are reputation effects. Reputation is one of the main reasons why companies are adopting Codes of Conduct in the first place. They want to persuade the customers that their products and services are produced in a socially responsible way.¹⁰ In a supply chain perspective, however, the company's wish to be seen as socially responsible is not necessarily shared by the other actors in the chain. Therefore, compliance with codes will be affected by these actors' interest in keeping a reputation as reliable transaction partners.

The reputation of a supplier can be seen as a resource, which influences future income (Koch, 1995, p. 16; Bensaou and Anderson, 1999, p. 469). For instance, if a supplier acts opportunistically, the buyer will probably not engage in future transactions. Moreover, the buyer might tell other companies that the supplier is an unreliable partner. On the other hand, there might also be costs associated with establishing and maintaining a reputation as an honest and trustworthy person (Ostrom *et al.*, 1993, p. 44). The supplier's choice of action therefore depends on a valuation of the costs and benefits from being a reliable partner.

¹⁰In an investigation of 246 voluntary Codes of Conduct, it was concluded that enhancement of the company's reputation and stronger customer loyalty was a strong motivation for implementing codes (OECD, 2000, p. 4). Moreover, in an analysis of Swedish firms introducing ISO 14000, 88.5% of the companies considered 'corporate image' as an important or very important motivation factor (Poksinska *et al.*, 2003, p. 593).

In the case of IKEA, reputation has proven an efficient safeguard. In the eyes of many of its suppliers, IKEA has an image as a 'tough' customer, which is in large part due to its IWAY requirements. Despite the fact that its tough requirements at times lead to complaints from the suppliers, IKEA also seems to benefit from its image as a tough and demanding customer. Thus, IKEA has experienced that several suppliers consider compliance with its IWAY requirements a good reference toward other (potential) customers, and consequently they are willing to go to great lengths to fulfil the requirements.

In conclusion, the applicability of reputation effects depends on the supplier's overall interest in keeping a good relationship with the buyer. Reputation is a highly relevant safeguard, when the supplier can benefit from future co-operation with the buyer, and/or the buyer can harm the supplier by communicating non-compliance to other relevant actors, for example in business networks. Relying on this protective mechanism requires an analysis of the power structures in the relationship, the characteristics of the transactions, and the external environment.

Conclusion: managing codes of conduct in global supply chains

Codes of Conduct can be seen as a contract between the company and society. The company promises to fulfil its societal obligations as a corporate citizen by being profitable, law-abiding and ethical (cf. Carroll and Buchholtz, 2003, p. 40). In a global supply chain perspective, however, where part of the production process is outsourced to companies in different geographic, cultural and institutional settings, such a promise cannot be made without the active commitment of all actors involved. However, Codes of Conduct are often vague and poorly monitored, which leaves some room for interpretation—and opportunism in the form of non-compliance.

Realizing that this non-compliance constitutes a threat to the companies, which promote themselves as socially responsible by developing Codes of Conduct, it is becoming increasingly

important to develop new means to manage and control inter-organizational relationships.

In the previous sections, this article has discussed some of the problems, which are associated with ensuring code compliance throughout the chain, and has tried to give an overview of some of the basic protective mechanisms, which can safeguard the buyer from non-compliance with Codes of Conduct in global supply chains. The discussion of safeguards can be summarized into a number of general recommendations to companies implementing Codes of Conduct in global supply chains:

- Direct sanction is a very effective safeguard if the buyer is the dominant partner in the business relationship (Unless non-compliance is very likely to go undetected, of course) (Koch, 1995, p. 14). The governance of code implementation can be relaxed if the exchange relationship is very important to the supplier (cf. Hill and Jones, 1992, p. 135). An analysis of the power structure and the resource dependency in the chain must be included in the planning of safeguard mechanisms. A description of legitimate direct sanctions should be included in the formulation of a Code of Conduct.
- Metaphorically speaking, direct sanction/exit is the stick whereas a bottom up/voice approach can be seen as the carrot (Helper, 1990, p. 6). Codes of Conduct are often implemented in a top-down way, but an increased involvement of the supplier in the planning and implementation of the codes might reduce the risk of opportunism because it aligns interests and establishes commitment to the initiative throughout the supply chain.
- Goal congruence can be achieved through joint investments and/or medium and long-term delivery contracts conditioned by code compliance. For instance, the buyer can support investments in socially and environmentally friendly technology and offer training and technical assistance in social and environmental management.
- Trust can be an effective safeguard, especially in long-term relationships in which the buyer and the supplier have accumulated a thorough knowledge of each other. However, it is difficult to separate opportunistic and trustworthy suppliers, and therefore trust must be combined with other safeguards.
- Third-party monitoring and enforcement can be an effective protective mechanism. Moreover, third-party verification can be a means to improve the overall credibility of the codes. Codes of Conduct are often met with some scepticism, and failure to ensure compliance with the codes might erode the overall credibility of the buyer's voluntary initiative. In general, third-party involvement can be recommended in the implementation of Codes of Conduct.
- Reliance on reputation effects depends on the costs and benefits of opportunistic behaviour. Reputation is a highly relevant safeguard when the supplier is dependent on future co-operation with the buyer, and/or the buyer can harm the supplier by communicating non-compliance to other relevant actors, for example in business networks. As with direct sanctions, the planning of code-compliance mechanisms requires an analysis of the relationship with the suppliers in the chain.

Future research

It could be argued that successful implementation of Code of Conduct requirements at suppliers not only depends on the type and scope of safeguarding mechanisms employed by the buying company but also on the ability of suppliers to adopt the necessary CSR practices in their own organization. Therefore, future research into CSR in supply chains may preferably include examinations of the suppliers' ability to receive and interpret the requirements from the buyer. Some studies already exist, which deal with the challenges and barriers experienced by suppliers—particularly suppliers in less developed countries—in the process of

implementing the environmental and social requirements of their buyers (Business for Social Responsibility, 2001; World Bank, 2003b). These studies reveal the existence of several issues, which could be investigated further so as to gain a more comprehensive picture of the complexities related to working with CSR in global supply chains.

A second issue to be researched further is the applicability of safeguarding mechanisms to small and medium-sized companies. Today, most companies working systematically with Codes of Conduct are large multinational companies. However, in a Scandinavian—and even European—context, the majority of companies are small and medium-sized. Even though an increasing number of small and medium-sized companies seem to work with Codes of Conduct, we may argue that they often lack bargaining power as well as financial and human resources, which are often necessary for safeguarding a Code of Conduct. Accordingly, future research regarding CSR in supply chains should concentrate on examining the potential of small and medium-sized companies of safeguarding CSR requirements.

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