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Mares, Radu

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LUND UNIVERSITY

PO Box 117  
221 00 Lund  
+46 46-222 00 00

# **RAOUL WALLENBERG INSTITUTE**

OF HUMAN RIGHTS AND HUMANITARIAN LAW

## **BUSINESS AND HUMAN RIGHTS**

Policy developments in six policy channels

**BRIEF 3/2017**

**AUTHOR: Dr. Radu Mares**

The 2011 UN Guiding Principles on business and human rights (UNGPs) have become the normative reference point for states, companies and civil society groups. Under the UNGPs businesses have a responsibility to respect human rights and exercise human rights due diligence. The question now is how to implement the UNGPs, including in terms of adding ‘teeth’ to the UNGPs through hard law and other policy measures.

Traditionally under international law, infringements of human rights by private actors like businesses trigger the responsibility of the state for its failure to prevent and remedy harm within its jurisdiction. However some states are unable or unwilling to prevent and redress such infringements as multinational enterprises operate globally through complex organizational and contractual structures. A regulatory gap emerges in which corporate irresponsibility thrives. The common approach of the corporate accountability movement has been to look at the top of the supply chains (or global value chains (GVCs)): invoke the responsibility of lead firms – parent or outsourcing companies –, and advocate for coercive legal solutions to hold them liable and obtain remedies for victims. This has been the unsuccessful project of “moving liability upwards” the GVC (Brief 1/2017). Adopting strong regulations in a transnational context to secure human rights throughout GVCs remains difficult (Brief 2/2017).

The six-year Ruggie mandate that concluded with the UNGPs broke with this project of “moving liability upwards” and its heavy reliance on coercive laws. The thinking behind the UNGPs urged that the field of vision be expanded beyond the top of the GVC; furthermore it accounted for legal and non-legal incentives to achieve more responsible conduct and ensure respect for human rights. This could be dubbed the “harvesting leverage” project of the UNGPs (Brief 1/2017). Arguably this project is more attuned to the challenges of regulating transnationally such complex systems as GVCs. However, the UNGPs left the task of how to regulate multinationals for another day; they were not meant as a blueprint for a stronger regulatory regime to tackle irresponsible business conduct.

The decade-old search for effective regulatory solutions to corporate unaccountability is happening nowadays in a changing context: the UNGPs offered a new conceptual foundation and there are recent policy developments worth taking into consideration. This brief tracks developments in a six policy areas:

- International trade law
- International investment law
- International human rights law
- Development cooperation
- Corporate social responsibility (CSR)
- Home-state regulation of lead firms

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**Note:** This brief draws on R. Mares, ‘De-centering human rights from the international order of states - The alignment and interaction of transnational policy channels’, *Indiana Journal of Global Legal Studies*, Vol. 23:1 (Winter 2016) pp. 171-199, available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2920756](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2920756).

The brief begins by showing the capacity of these six policy areas to shape business conduct throughout GVCs. While these developments are remarkable, they reveal a scarcity of coercive laws. The question, is then, how to reason about these recent developments and their potential for human rights protection? Should they be criticized and dismissed as weak? If not, how could these developments matter and change corporate conduct when the profit-making motive and market pressures are so strong?

The brief argues against evaluating the developments in these six channels on only one indicator of coerciveness; it cautions against premature dismissal just because they are not coercive enough. The proposal here is that we should track three indicators: strength (coerciveness), depth (root causes) and tightness (interaction) of channels. In short, these developments might be judged differently when seen together rather than in isolation, especially if they begin to acknowledge and tackle deeper causes of the problems in GVCs.

## SETTING THE ANALYTICAL STAGE

The UNGPs explain there are different levels of involvement in harm that trigger a company's responsibility to act. Thus the UNGPs spell out three settings — causation, contribution, and linkage — that trigger the responsibility to respect human rights.

**The responsibility to respect human rights requires that business enterprises:**

- (a) Avoid causing or contributing to adverse human rights impacts through their own activities, and address such impacts when they occur;
- (b) Seek to prevent or mitigate adverse human rights impacts that are directly linked to their operations, products or services by their business relationships, even if they have not contributed to those impacts

Source: UNGPs (2011), Principle 13

Two aspects should be highlighted here: the root causes of human rights infringements in the value chain and what the responsibility to act requires more specifically.

## Root Causes of Infringements in Global Value Chains

When looking at GVCs, there could be two types of root causes to human rights infringements: one lying squarely with the lead firm<sup>2</sup> and its wrongful decisions (Type 1 cause), and another root cause having to do with the affiliate and the host country's legal regime (Type 2 cause).<sup>3</sup>

**Type 1 root cause:** a business (lead firm) might make decisions that have ripple effects throughout the value chain. Examples can be the decisions of investors to set up or instruct a subsidiary operating in a high risk zone without taking necessary precautions. Another example can be the decisions of buyers to change product specification on short notice; or, more broadly, to devise sourcing arrangements that rely on flexibility, fast turnaround and low costs, which create downward pressures on suppliers. The foreseeable consequence

<sup>2</sup> Lead firm has influence or even control over some entities in the global value chain, such as subsidiaries, contractors, suppliers.

<sup>3</sup> Root cause analysis is meant to convey the importance of a thorough investigation of less visible factors leading to infringements of human rights. That renders HRDD as a process that is in-depth and comprehensive addressing underlying causes instead of treating mere symptoms.

of such decisions is human rights being infringed.

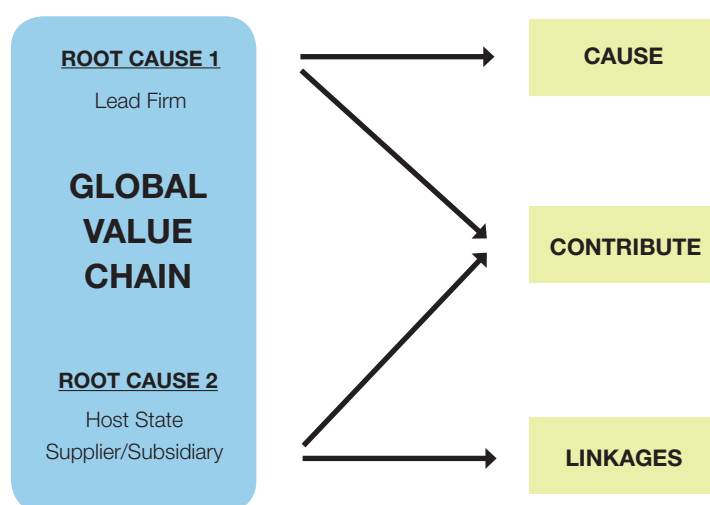
In the UNGPs, such decisions appear as ‘contribution’ to harm, occurring in partner(s) operations. Therefore a business cannot obscure a root cause under its control and deflect responsibility by blaming the harm solely on its affiliate. A company should take measures to prevent such wrongful conduct from occurring and make sure it remedies the harm it caused or contributed to. In short this is a responsibility for direct involvement in abuses in the GVC.

**Type 2 root cause:** a business might be linked to harm by virtue of doing business with an abusive partner. The root cause here is to be found in the wrongful conduct of the partner and the failings of the host country’s regulatory regime. According to the UNGPs, the business cannot separate itself too easily from this root cause just because it did not cause the harm through its own culpable decisions. The business is still linked to adverse impacts through its business relationships, and that triggers the responsibility to act to ensure respect for human rights.

Under the UNGPs, there are multiple modalities to address Type 2 causes. Thus the business is first expected to exercise leverage and ultimately to terminate the relationship if exercising leverage leads to no improvements (Principle 19). In short, the company cannot disclaim Type 2 causes and pursue business as usual by, on the one hand, resorting to legal technicalities, such as limited liability regarding its subsidiaries and not owning the supplier or, on the other hand, pointing to practical difficulties of having limited leverage on the host state or the affiliate. In short, the business has a responsibility for its indirect involvement in abuses in the GVC.

The notion of leverage is important for understanding the corporate responsibility for indirect involvement, as above, but also for the entire Ruggie project of harvesting leverage from all possible sources to secure human rights. This brief goes further to show how leverage of six policy channels has recently increased and might get compound if the channels align and interact.

**Figure 1: Two Root Causes of Infringements in Global Value Chains**



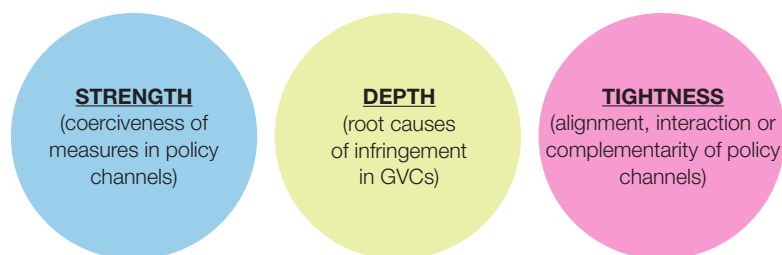
### Three indicators for measuring recent developments

The increasing integration of national economies through international trade and investment presents risks that economic interests will trump human rights concerns, but also new opportunities to address both of the aforementioned root causes. It should be clarified already here that state obligations under classic international law remain equally relevant as before. Similarly hard law and coercive measures remain an essential tool to achieve compliance, particularly for direct involvement cases. But given the difficulties encountered in regulating transnational business operations (Briefs 1 and 2/2017), it is essential to account for new sources of leverage and new pathways toward human rights protection.

This section highlights developments in six transnational policy channels. These developments could be dismissed as weak and insufficient, and in some cases as diverting attention from the harms done by some channels (e.g. trade, investment). Therefore, nothing short than coercive regulations and reform of entire channels suffice or matter. This brief offers an alternative approach in line with the ‘harvesting leverage’ project behind the UNGPs. Whether coercive or less coercive mechanisms are at play should be clearly noted when examining policy developments related to GVCs. This however should be the beginning, not the end, of the inquiry regarding ways forward.

Therefore strength (coerciveness) is only one indicator of the emerging governance regime for corporate accountability: the other two are depth (root causes) and tightness (interaction). Depth seeks to capture the evolution of channels beyond superficial policies towards acknowledging and addressing deeper causes of problems. Tightness impresses that policies in the six channels are evolving in a denser regulatory space rather than in isolation and oblivious of the other channels; there are indications of a shift towards alignment of channels. Thus in examining policy developments related to GVCs, the main interest is on whether these channels address root causes and whether these policy channels demonstrate actual or potential alignment, interaction or complementarity. The remaining of the brief tracks these three indicators in six policy channels.

**Figure 2: Three Indicators**



### TRANSNATIONAL POLICY CHANNELS

The quest for respecting human rights in transnational business operations cannot afford to waste any source of leverage. Therefore the analytical framework should not prematurely discard policy channels that carry less coercive forms of leverage. Indeed the premium is on valorizing all sources of leverage along GVCs. There are some seeds for optimism, precedents, and experiments coming to maturity in the policy areas analyzed.

## Channels 1-2: Economic Inter-State Channels

**International Trade law.** The link between trade and labour rights was hotly debated in the mid-1990s when the World Trade Organization (WTO) was being set up. Developing countries feared protectionism and threats to their competitive advantage based on low labour costs. This foreclosed labour aspects within the WTO and relegated them to the International Labour Organization (ILO).

Somehow unexpectedly, the link between trade and labor/human rights began to flourish since the mid-2000s at the levels of bilateral and regional free trade agreements (FTAs). In parallel, labour and human rights clauses continued to feature in the development-driven General System of Preferences (GSPs) systems set up in the 1970s to give less developed countries access to rich country markets on preferential terms (unilateral trade agreements).

### Social clauses in trade agreements

- Trend: From 4 (1995) to 58 (2013) to 75 (2016) FTAs with labor clauses
- Growing trend: 80 per cent of FTAs entering into force since 2013 include labour clauses.
- Content of social clauses: the state either commits to not lower and to enforce existing domestic labor laws, or to pass laws based on ILO standards.
- 60% of FTAs are exclusively promotional and 40% are conditional (sanctions or benefits)
- Dispute resolution mechanisms: rarely activated

Sources: *ILO, Social dimensions of free trade agreements (2013)*; *ILO, Assessment of labour provisions in trade and investment arrangements (2016)*

By requiring exporting states to improve their labour governance, the international trade channel targets Type 2 root causes (host state laws). Suppliers involved in global value chains would be encouraged and compelled by host state regulation to respect labour rights in order to access global markets on the advantageous terms set in trade agreements.

The proliferation of FTAs – bilateral or regional – is a notable development. But how strong are these references to labour rights in FTAs? The bulk of implementation efforts are of a cooperative rather than coercive nature, so they score low on the strength indicator. The trade law channel delivers leverage towards Type 2 root causes as it seeks to reorient exporting states and exporting companies strategies of integrating in global markets, so they score high on depth indicator. Thus FTAs direct leverage at a root cause but at the same time it is a limited leverage. The latter could be augmented either by changing towards more coercive clauses or through alignment and interaction with other policy channels. What do these FTAs reveal in terms of interaction with other channels?

By requiring cooperation and support for exporting states, the trade channel aligns naturally with development aid and human rights law, as both channels aim to strengthen the capacity of host-state institutions to devise and implement adequate labor laws. Furthermore, the European Union has put forward its “values-based trade agenda”; its focus is explicitly on global value chains and demonstrates a positive disposition to intervene both at the top and bottom of GVCs.

#### **EU's 'Values-based trade'**

- 'The EU's trade and investment policy must respond to consumers' concerns by reinforcing corporate social responsibility initiatives and due diligence across the production chain...'
- Responsible management of global supply chains – 'essential to align trade policy with European values. [These policies] are complex and must involve a range of public, private and civil society actors to make meaningful changes for people on the ground. They also involve a mix of soft and innovative tools and legislative changes.'
- Promoting fair and ethical trade schemes – 'reflects EU consumer demand and contributes to developing more sustainable trade opportunities for small producers in third countries.'
- Trade policy – 'a powerful tool to further the advancement of human rights in third countries in conjunction with other EU policies, in particular foreign policy and development cooperation.'

Source: EU, *'Trade for all – Towards a more responsible trade and investment policy (2015)'*

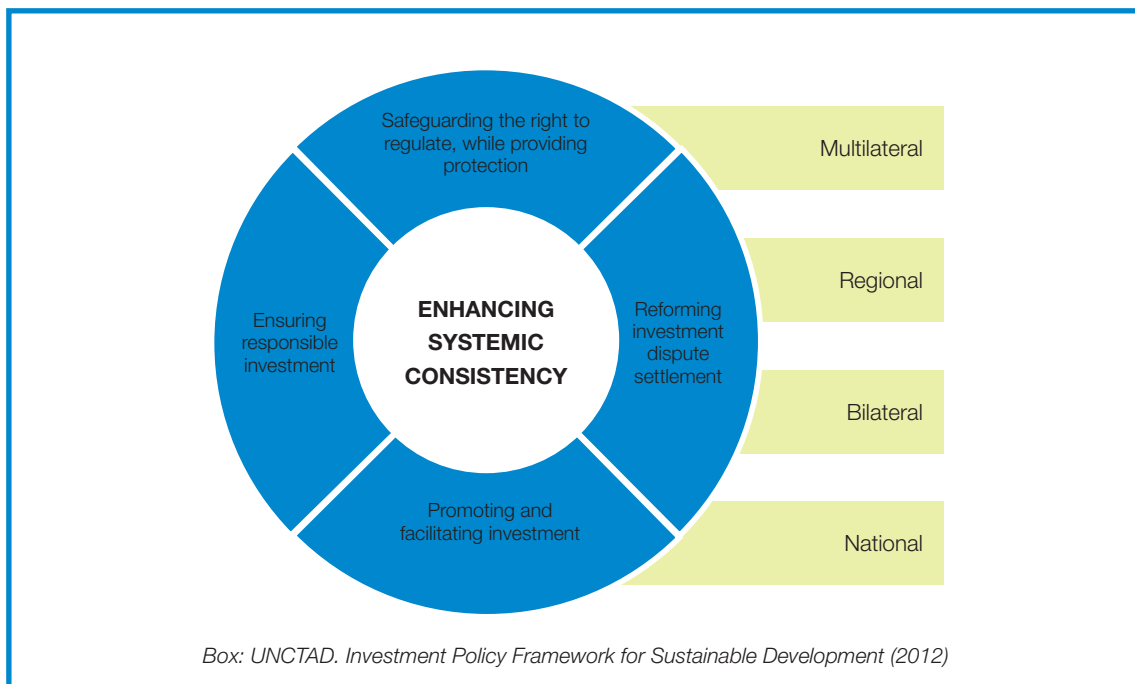
The above points to an emerging alignment of transnational channels. Historically the macro and micro levels of trade governance have developed separately. Thus the debates on the macro-level of trade law focused on reducing tariffs on goods crossing borders. In the same time the micro-level of trade contained top-down efforts by multinational enterprises (i.e. CSR) as well as bottom-up efforts by suppliers to gain private certification (i.e., fair trade regimes). By now, modern trade law has expanded beyond tariff-reduction, and CSR has evolved beyond simplistic audit-your-supplier approaches. The area of alignment around labour rights between the macro and micro levels of trade governance is thus enlarging.

**International Investment law.** Compared with international trade law, investment law raises different concerns from a human rights perspective; rather than facilitating access to global markets for exporting states through reduction of tariffs, investment treaties offer foreign investors special protections enforced through international arbitration for issues such as expropriation and unfair treatment. Currently there are over 3,000, bilateral investment treaties (BITs) since the 1960s.

Following heavy criticism, the EU and UNCTAD are leading the way to address the excesses of the BITs. The reform seeks to safeguard the host state's right to regulate and adjust the international arbitration mechanism. The question is whether the human rights responsibilities of investors could be incorporated in BITs and acquire thus legally binding status. Some BITs already make reference to CSR though falling short of establishing enforceable obligations. Such CSR references create an opening: less coercive for now, but conceivably could evolve towards more coercive forms given the unique international arbitration mechanism accompanying BITs. That would address Type 1 root causes.

Equally important, revised BITs would reaffirm the host state's right to regulate and thus address Type 2 root cause: that would remove a disabler from the business and human rights equation by allowing, if not obliging host states, to discharge their human rights obligations under international law through proper regulation of businesses.





In sum, measuring just the coerciveness (strength) indicator would make it easy to discard the trade channel as ‘soft’ and unfit to protect human rights and to dismiss recalibrations in investment law as inconsequential or deceiving. However that would be premature and foreclose needed inquiries given that other transnational policy channels are at play addressing the same root causes (depth) and display alignment and interaction tendencies (tightness).

#### Channels 3-4: Human Rights-Related Inter-State Channels

**International Human Rights Law** (IHRL) has relied on ratifying states to respect and ensure human rights within their (territorial) jurisdiction. Thus it is a tailor-made regime to address Type 2 root causes. There are new developments supplementing this traditional focus on host states. One of them is the movement to emphasize the extraterritoriality of home state obligations. That would trigger new laws concerning lead firms’ global operations and impact on Type 1 root cause.

Another development is the way that the UNGPs enabled the UN human rights machinery to question states for failing to ensure that companies employ human rights due diligence. Thus the UN Special Rapporteurs and treaty bodies regularly use the UNGPs in their dialogue with states; both Types 1 and 2 root causes are addressed. Furthermore, the current discussions in the UN regarding a treaty on corporate human rights responsibilities will be a revealing moment. As indicated above, the UNGPs are based on a more complex strategy to transnational economic activity than previous UN attempts to regulate MNEs, which proved unsuccessful (Brief 1/2017). As a result IHRL might develop new ways of regulating GVCs in a more ‘polycentric’ manner and thus emphasize alignment and interaction among several policy channels.

Overall, the IHRL channel has been traditionally deprived of coercive mechanisms, but nowadays it seeks to maximize its leverage: it is expanding its focus beyond host states’, human compliance and is sharpening its focus on the human rights impacts of business operations. In the process, IHRL targets both Types 1 (in home states) and 2 (in host states) root causes as these states fail in their obligations to protect human rights by regulating parts

of the GVC. At the same time, IHRL continues to offer the detailed understandings of human and labour rights that are being employed as reference points by other policy channels.

**Development cooperation** has for a long time referred to rule of law, democracy, human rights, and good governance. In this way, the official development assistance (ODA) channel has targeted the human rights performance of host states (Type 2 root causes). That was achieved either through developed countries offering economic aid backed by human rights-related conditionalities or through directly supporting institutions relevant to human rights. Thus the ODA channel featured the full spectrum from capacity-building to coercion through (negative) conditionalities to promote human rights.

As the developmental paradigm shifted away from state-driven development models, the ODA has concentrated increasingly on private sector development and on linking local businesses to international markets. This led naturally to the ODA supporting CSR. For almost two decades the ODA has supported responsible supply chain management. Support has gone to different strategic points of the value chain: directly to suppliers seeking better access to international markets, to corporate accountability NGOs, to multistakeholder CSR initiatives, and to CSR standardization efforts.

Finally, the ongoing alignment of the ODA with the modern trade law agenda, as exemplified by the EU policies, has increased as trade expanded beyond reducing tariffs to issues of institutional strengthening in relation to labor rights, environmental protections, rule of law, and regional integration. For example, Better Factories Cambodia (BFC) demonstrates the alignment and convergence of different channels to address a Type 2 root cause.

Triggered by the US-Cambodia Textile Agreement (1999), BFC delivered a locally protective arrangement for Cambodian workers. The BFC attracted the involvement of the ILO and the International Finance Corporation (the IHRL and ODA channels) as well as that of international buyers (the CSR channel) that relied on the credible audits performed by BFC.

#### **Better Factories Cambodia**

- Covers 500 factories and 530,000 workers (2015)
- Three services: 1. Assessment of factory compliance 2. Strengthening factory-level social dialogue; and 3. Training
- Transparency Database - covers 70% of Cambodia's export garment factories
- Collaboration with the Ministry of Labour, Ministry of Commerce, Garment Manufacturers Association in Cambodia, trade unions, and 37 international brands
- 'Building a responsible and competitive industry requires patience, commitment, and the involvement of a variety of stakeholders working together to tackle challenges and formulate solutions at the factory level, across the sector and throughout supply chains'

Source: *Better Factories Cambodia Brochure* (2015)

<http://betterfactories.org/cambodia/wp-content/uploads/2015/09/BFC-brochure.pdf>

In sum, both IHRL and ODA channels have had a direct bearing on inadequate regulatory regimes in host countries. Such channels relate easily to the Type 2 root cause of harm and more recently on Type 1 causes as well. Conditionalities aside, both channels fall short on

coercive mechanisms to shape state and business conduct. However both IHRL and ODA are finding new ways to relate to other policy channels and increase their leverage.

## **Channels 5-6: Intra-firm Channel**

**Corporate social responsibility** (CSR), the policies of lead firms that voluntarily address their impacts, has evolved in the last 20 years. There are now progressive CSR strategies that increasingly reveal a root-cause orientation in “diagnosing” human rights infringements down in their supply chains and “curing” those infringements through alignment-of-channels strategies. Both Types 1 and 2 root causes are addressed.

Regarding Type 1 causes, there are now frank admissions from some lead firms about how their own practices contribute to infringements throughout the GVC. This frankness makes it disingenuous for other businesses to shift the blame wholesale to the affiliate (a supplier’s social irresponsibility) or to the host state (government inability or unwillingness to regulate suppliers). These are acknowledgements of the ‘downward pressures’ on suppliers created by lead firms in a general context of intense market competition to which suppliers are subjected.

### **The root causes of excessive overtime**

Nike: “During FY11, more than two-thirds (68 percent) of the excessive overtime incidents identified and analyzed through audits of 128 factories were attributable to factors within Nike’s control, primarily forecasting or capacity planning issues, shortened production timelines and seasonal spikes.”

Source: Nike, Inc. *FY10/11 Sustainable Business Performance Summary* (2012) p. 53

Advanced CSR strategies combine measures targeting both Types 1 and 2 root cause in GVC. An example is the issue of living wages in Cambodia’s textile industry. The approach of H&M and other brands defines expressly the role of buyers vis-à-vis the host government and unions. The aim is to facilitate a mature industrial relations system by collaborating with the ILO and the Swedish development agency. Such a strategy addresses Type 2 root causes, as it puts government, local employers, and labor on notice that it is not the foreign buyers’ role to set wage levels. However, these buyers have not overlooked Type 1 root causes: these brands made a commitment to keep sourcing as long as local parties are committed to settling the wage issue. This commitment is essential as it tackles the possibility of buyers redirecting purchasing orders – a facile compliance strategy for buyers to separate themselves from abuses – and thus enables local actors to improve. This removes a significant disincentive for suppliers and the host government, fearful of diminishing the international competitiveness of their industry.

As to Type 2 root causes, complex strategies are being pursued. The Rana Plaza factory collapse that killed 1,127 workers in Bangladesh in 2013 triggered responses through multiple channels. There were two industry responses: the Accord and the Alliance. In addition, the European Union, the ILO, and the government of Bangladesh reacted with a “Sustainability Compact” in 2013. Also the ILO-IFC Better Work Programme, building on the above-mentioned Better Factories Cambodia, was introduced in Bangladesh. These initiatives take notice of each other and seek complementarity in addressing health and

safety issues as well as their root causes.

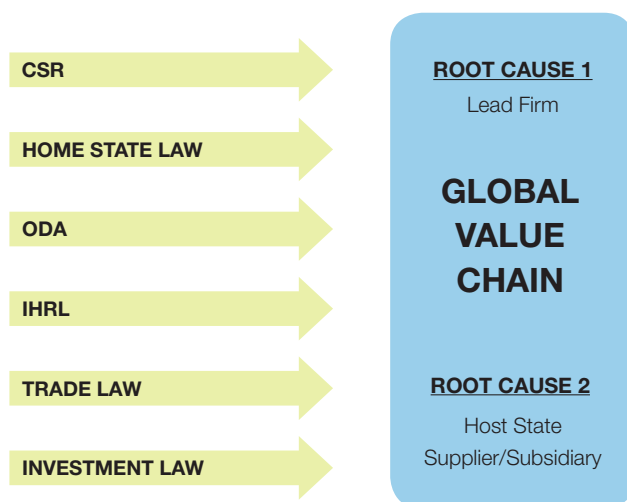
**Home-State Regulations.** A range of regulations in home states have recently appeared that target the conduct of lead firms. The most prominent example are transparency laws that cover social and environmental impacts of corporate activities, both at home and abroad. The 2014 EU Directive on non-financial reporting is an example. Although a legal requirement, the route between such transparency laws and respecting human rights is tortuous; coercion is indirect and uncertain as it will come primarily from societal and market actors, not from courts or regulatory agencies. This is a less coercive legal approach. Such laws start a dialogue, prompt corporate learning through self-assessments inherent in preparing a public report, and facilitate societal mobilization towards both Types 1 and 2 root causes. Even the pioneering ‘duty of vigilance’ law adopted in France in 2017 – making human rights due diligence mandatory for large companies – is less coercive than might appear at first glance.

States are also buyers in the area of public procurement, and financial actors in investments, credits, and guarantees for companies operating abroad. Through contracts, states are in the position to apply leverage at the top of GVCs by requiring business to demonstrate that they undertook human rights due diligence. Again, both Types 1 and 2 root causes get addressed.

There is also the angle of transnational litigation based on civil or criminal laws targeting the GVC at the top. Such legal strategies are coercive and target Type 1 root causes, but cover only a narrow band of situations given that they require strong involvement of the lead firm (own culpable conduct) in the affiliate’s abusive operations (Brief 2/2017). Overall, outside such direct involvement, cases of parent companies, the legal picture remains one of less coercive transnational regulations.

In sum, there are more mature forms of CSR that display a root-cause orientation and a search for more complex solutions, revealing thus alignment and interaction with other policy channels to maximize leverage over root causes. The recent laws of home states are notable developments, and can address both types of root causes, but tend to take less coercive forms.

**Figure 3: Multi-channel model**



**Implication 1.** Developments in six transnational channels. Advances in these channels that shape the governance of GVCs should not be ignored or quickly downplayed just because they do not take the shape of coercive laws. Discarding prematurely some transnational channels risks wasting valuable leverage that the transnational protection of human rights cannot afford. The project is one of harvesting leverage and finding ways to valorize less coercive strategies to shape business conduct.

**Implication 2.** Three indicators to be tracked. Transnational policy channels should be examined for root cause orientation and interaction with other channels. This allows measuring recent developments for depth (root causes) and tightness (interactions) in addition to the current emphasis on strength (coerciveness) of each channel.

**Implication 3.** Against isolated assessments. Recent policy developments could be assessed in isolation, one by one, and criticized for being weak in regulatory terms. Adding new dimensions – interactions and root cause orientation – allows new evaluations of policy developments and a wider variety of regulatory options. A policy channel displaying less coercive legalization should not be summarily dismissed or relegated to worthless unless it evolves into coercive law.

**Implication 4.** There is a choice regarding the direction for legal innovations. Corporate accountability proponents can set their eyes at the top of the GVC and seek to employ coercive means against lead firms (the project of ‘moving liability upwards’). Or proponents can expand their field of vision laterally to policy channels that impact on GVC, including through less coercive means, and seek to make sense of their regulatory significance (the project of ‘harvesting leverage’ throughout the GVC). The implications for the regulation of lead firms and GVCs are detailed in another brief (Brief 4/2017).

**The brief identified two root causes of abuses in transnational operations: a lead firm’s own decisions (top of the chain), and the supplier irresponsibility and host state weakness (bottom of the chain). There are six transnational policy channels that bear on these two root causes. Recent developments in these channels create openings to harvest and direct leverage at root causes, but also reveal a scarcity of coercive legal strategies. The brief argued against premature dismissal of these developments and against evaluating them based on only one indicator of coerciveness. Instead evaluations should track three indicators: strength (coerciveness), depth (root causes) and tightness (interaction).**