

Going Deep

The case for multi-tier transparency - November 2013



Executive summary

This briefing makes the case for a multi-tiered approach to responsible supply chain management. It highlights some of the pitfalls in failing to look beyond first tier suppliers and includes a snapshot of how far some leading companies are looking down their supply chain. Recommendations and case studies to help more companies achieve a deeper dive in their management of supply chain risks are also provided.

Key points:

- Globally, only a third of companies are actively seeking transparency below tier 1 in their supply chain, at scale.
- The greatest and most critical sustainability risks are found deeper down the supply chain.
- Companies that reach past the first tiers improve supply chain management and meet stated business and sustainability objectives.
- Supplier relationships built on engagement, trust and empowerment are central to managing supply chain risks.

Why transparency

Pressure on companies to understand their global supply chains is rising, but is nothing new. The scandals faced by Nike in the 90's are being endured today by Apple and Foxconn. Media-savvy stakeholders are pushing companies toward greater transparency and asking why we aren't seeing real improvements.

New legislation and frameworks, alongside greater media attention, place the spotlight on global supply chains. The UK Bribery Act, Dodd-Frank Act, California's Transparency in Supply Chains Act and international frameworks, such as the UN Guiding Principles for Business & Human Rights, are just a few of the recent developments, which advocate a proactive and multi-tier, due diligence approach. Important stakeholders from socially responsible investors to NGO's effectively coordinate new and old media to highlight poor performers whose suppliers operate with questionable labour and environmental practices.

Whilst multi-tier transparency is challenging, leading companies are using better data from deeper in the supply chain to enable more robust risk management and to build more resilient supply chains. Companies that monitor and understand supply chain data can more quickly assess and mitigate risks. They can also identify positive trends, replicate good practice, build a web of supply chain partners and sustainability champions; allowing companies to quickly identify supplier sustainability needs.



The top 2 most important actions for businesses to take to build public trust are to **“increase transparency of business practices”** and **“measure and demonstrate positive social and environmental impacts.”**

Source: BSR State of Sustainable Business Poll (2012)

“Almost 40% of CDP members report financial savings from their emissions reduction activities. More than a 1/3 have benefited from new revenue streams or from savings gained as a result of their suppliers' carbon reduction activities.”

Source: Accenture

Critical risks increase down the supply chain

Supply disruptions “**significantly impact business and financial performance**” but nearly **two thirds of companies pay only “marginal attention” to supply chain risk reduction**, according to a 2013 study by PwC and MIT. Engaging the first tier is a vital place to start as it is where businesses have the greatest, direct influence. However, this is only the first step of a proactive supply chain management programme.

Sedex - provider of the world’s largest collaborative platform for managing and sharing multi-tier supply chain data - analysed data from ten companies who we have identified as achieving extensive engagement throughout their supply chain tiers.

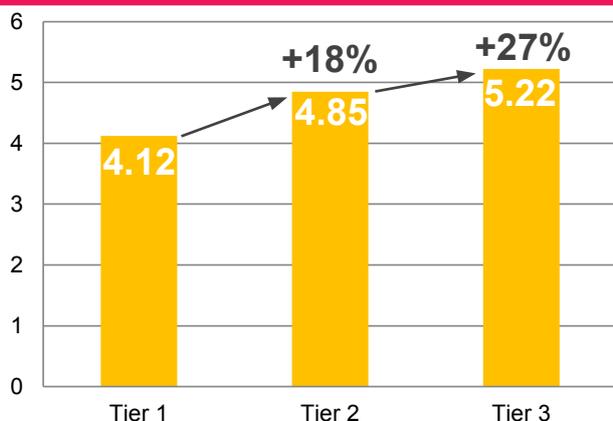
This unique study shows that risks clearly increase further down the supply chain. At tier two, site audits identify an average of 4.85 non-compliances (NCs) per audit – 18% more than the number of NCs identified in tier one (Figure 1).

As figure 1 shows, the number of NCs rises beyond tier one, but are most significant at tier three, which represents just 7.3% of trading relationships yet raised 27% more NCs per audit than tier one, on average. The criticality of issues also increases in sub-tiers with tier three showing the highest number of issues (Figure 2).*

In engaging with suppliers, companies often prioritise those with which they have a higher spend or who pose a higher risk. As tier one suppliers are often the first place to start supply chain management programmes, these companies have had more time to address issues than those further down the supply chain.

By taking a multi-tiered approach, the ten companies included in our sample achieve greater engagement with their suppliers and better insight to more effectively understand, monitor and tackle risks head on.

Figure 1: Average number of NCs per audit per tier from the sample of 10 companies
(shows the average # of NCs per audit in each tier.)



The sample analysed 10 companies with a combined total of 3,922 supplier relationships and 6,775 audits.

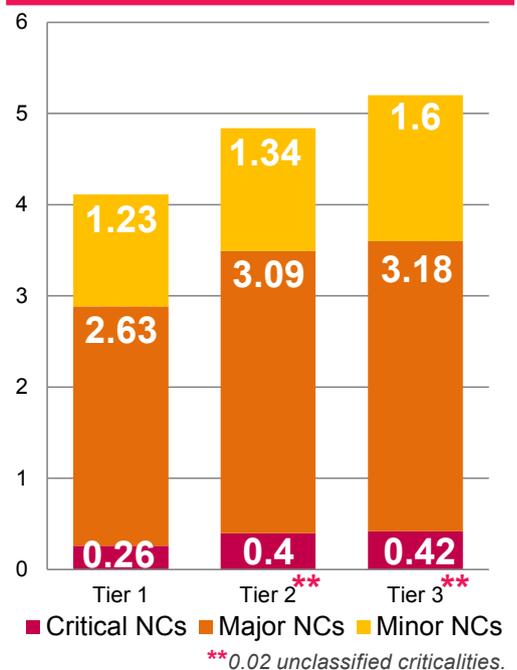
* In a bid to create a consistent list of critical issues for members to focus their resources and efforts effectively Sedex provides guidance documents to members and auditors to promote consistency in approaches via SMETA (Sedex Members Ethical Trade Audit).

- **Critical NC:** a severe breach which presents imminent risk to workers safety /risk to life and limb, or constitutes a significant breach to workers’ human rights, or an attempt to pervert the course of the audit through fraud, coercion, deception or interference.
- **Major NC:** a breach which represents a danger to workers /those on site or systematic breaking of a code requirement/law.
- **Minor NC:** an occasional or isolated problem or an issue which represents low risk issues to workers /those on site.

Key insights

- **Multi-tier transparency is possible:** Our sample proved that companies are achieving engagement with 44.5% first tier, 47% second tier and 7.3% of third tier suppliers.
- **Risk is higher beyond tier 1:** Our sample found that the second tier raises 18% more NCs per audit, and the third tier raises 27% more NCs per audit than tier one, on average. It also shows that the criticality of issues is higher in the deeper tiers of the supply chain.
- **More visibility enables risk management:** Tiers two-three hold even higher NC’s than tier one, on average; making evident that multi-tier transparency is necessary to properly understand supply chain risk.

Figure 2: Breakdown of the average level of NC criticality per tier
(shows the average numbers of issues raised by issue criticality by tier)*





BSR Perspective: Supply chain transparency is an opportunity that should be seized

Mapping your supply chain and adopting a multi-tier approach offers multiple business benefits.

Consider the importance of multi-tier transparency for companies with minerals in their supply chains. The OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High Risk Areas identifies the numerous steps and actors in complex supply chains that involve mining or trading in minerals; ultimately revealing that multi-tiered transparency right down to the smelter level is necessary to reduce risk of the most material sustainability risk issues for these supply chains.

From a corporate emissions perspective, often the majority of total emissions and the greatest carbon impacts for many products come from Scope 3 (indirect emissions) sources¹. In addition, while 90% of companies have targets for carbon reduction, only 38% of top suppliers do². As the supply chain accounts for between 50 - 70% of both total expenses and greenhouse-gas emissions for most manufacturing companies³ and most companies lack direct engagement beyond tier 1, it's vital that more companies engage suppliers to cascade good practice down the supply chain to achieve targets.



BSR Mills & Sundries Working Group

Getting to these lower tiers can uncover 'hidden' challenges and opportunities, both for major buyers and the suppliers in these lower tiers.

BSR's Mills & Sundries working group – a group of apparel and retail companies and suppliers working in partnership to reinforce mutual transparency and improve factory conditions - actively engaged with 800 tier 2-5 suppliers in the garment industry. This engagement uncovered various challenges including: excessive working hours in dye houses that require a 12 hour set time, improper water use in a laundry facility located in a drought region, and the impact of increasing cost of natural resources on factory production. By working collaboratively, the companies were able to reach more suppliers and uncover more hidden risks than they could have done alone. In addition, it provided better insight and buy-in.

The participating suppliers also gained. There was the direct value from interfacing with their end customers; but equally, the brand interest, investment, and guidance was helpful to suppliers not currently part of mainstream auditing schemes. As a result of participation, they became more prepared for future requests, more able to understand the issues within a shared environment with other similar suppliers, and developed their own voice and opinion to respond to challenges.

¹ GHG Protocol

² CDP 2013 Supply Chain Report

³ Accenture

Marks & Spencer: Gaining Transparency

Marks & Spencer knows their first tier suppliers well. *“We know the name of the owner, address and details of every single factory that produces our goods,”* says Fiona Sadler, Head of Ethical Trading.

The company also requires that first tier suppliers to cascade its Global Sourcing Principles and other information, down to the subsequent tiers, which enables the company to strengthen its relationships further down the supply chain. It requires all first tier sites where M&S product is made to be registered and sharing data via Sedex.

“We approve all sites and have audited and visited them. We think this is really important because if you don’t know where your factories are, it is impossible to have a true picture of what is happening in your supply chain,” Fiona says.

In addition, Marks & Spencer is part of many collaborative transparency initiatives, such as the Better Cotton Initiative, that enables a collaborative approach to gaining transparency at all levels in their supply chain.



Magrabi Agriculture, Egypt

Diageo: The challenge of scale

“At Diageo we talk about 70,000 suppliers and third parties, spread across over 100 countries of the world. When multiplied by the number of sub-suppliers in the supply chains, you get in to hundreds of thousands of people impacted by our global supply chain, so its vital to prioritise the key areas.”

David Lawrence, Global Compliance & Ethics Programme Director, Diageo

“Collaboration can help companies to tap into tiers of their supply chain that are difficult to reach. We know that much of the risk and opportunity in the supply chain lies outside of a company’s direct control, because it’s not with direct suppliers. By working together with others to pool knowledge and make contacts in these lower tiers, companies can get the transparency they need.”

Tara Norton, Director, BSR
tnorton@bsr.org

“Modern supply chains are vast, ever-changing networks that stretch across the world - this briefing underlines the huge challenges companies face in trying to achieve transparency and the importance systems and data play in helping companies manage and gain insight at scale. Research like this helps us understand how we can support a step-change to drive engagement from the bottom-up.”

Carmel Giblin, CEO, Sedex

Concluding remarks

Our research tells us that there are excellent examples of companies adopting multi-tiered approaches to supply chain management. However, we also see that:

- There is still significant work to be done to overcome the challenges of scaling-up supply chain management to achieve transparency beyond first tier suppliers.
- The number and criticality of issues increase further down the supply chain.

Click to take part in our poll
Supply chain transparency - how far are you looking?



Key Recommendations

Map your supply chain

- Look beyond the first tier to map your supply chain. Start by identifying and focussing on areas of known risk and the critical areas of your supply chain and/or individual suppliers that are of highest priority to your responsible sourcing strategy.
- Target high risk areas for greater data collection that provides transparency. Use systems that enable you to scale up your efforts to engage below tier 1.

Communicate effectively

- Engage with your direct suppliers, clearly state your companies' sustainability ambitions and expectations, why you need data from your supply chain, what the data will be used for and the business benefits for suppliers. Cascade down as appropriate.
- Be mindful that targeting suppliers for significant improvements or orders without realistic timeframes or support can have unintended consequences that are a risk to brand value and reputation.

Encourage transparency

- Establish a relationship with suppliers that is based on trust, which encourages and rewards transparency and honest reporting. Encourage ownership and innovation to meet sustainability objectives.
- Make sure your business processes respect suppliers and do not undermine your sustainability objectives. Train internal people so they understand what good and bad looks like, what impacts their decisions have and why.

Monitor the risks

- Use data to better understand the risks in your supply chain: segment suppliers, identify hotspots and trends, prioritise resources and effort, and track progress against commitments and targets.

Collaborate to gain collective transparency

- Engage in collaborative initiatives across multiple tiers down to raw material suppliers, to gain visibility and collect non-financial data on risks and opportunities.
- Provide support to these initiatives to empower and build the capability of your supply base at levels below the first tier.

About this briefing:

This business briefing is the latest in a series of films, publications, resources, webinars and in-person events by Sedex Global and partners. These focus on a range of topics including; key emerging trends for sustainable supply chains by region and emerging CSR topics, risk and performance management in global supply chains, highlighting companies' achievements of good practice and best practice, impact, collaboration and convergence in responsible business. See <http://www.sedexglobal.com/resources/publications/>

RESOURCES

Sedex offers initiatives and resources that help companies source responsibly, to fast-track transparency, and to demonstrate the business case for supply chain sustainability. These include:

SMETA (Sedex Members Ethical Trade Audit): an audit methodology that engages supply chain monitors, buyers and suppliers in one common audit approach, thereby reducing duplication and increasing convergence.

Responsible Sourcing Insights: six short films featuring interviews with leading multinationals, suppliers, trade bodies, NGOs and other experts at the sharp end of tackling responsible supply chain challenges.

Associate Auditors Group (AAG): a group of auditing companies, Sedex members, NGOs and other ethical auditing experts that work together to drive convergence in ethical trade/social auditing, based on, and helping to shape, best practice.

Sedex Supplier Workbook: an in-depth guide offering practical guidance, case studies and good practice to help suppliers around the world drive ethical improvements in their businesses.

Find out more at www.sedexglobal.com

Disclaimer:

Data covers July 2011 to August 2013. All data correct as of 10th September 2013.

About the partner author organisations:

Sedex Global (www.sedexglobal.com)

Our mission is to drive collaboration, increase transparency and build the capacity that's needed to raise standards across all tiers of the supply chain. We offer the world's largest collaborative platform for managing and sharing ethical supply chain data, along with leading-edge services which multi-national companies use to understand, monitor and manage supply chains risks and improve standards.

Sedex works to drive engagement up and down the supply chain, encouraging follow up corrective actions on audits and facilitating dialogue to address challenges 'on the ground'. We collaborate with a range of stakeholders to share insights and promote best practice on responsible supply chain issues.

Sedex offers a range of services to enable effective responsible supply chain management. See <http://www.sedexglobal.com/member-services/>

BSR (www.bsr.org)

BSR works with its global network of more than 250 member companies to build a just and sustainable world. From its offices in Asia, Europe, and North and South America, BSR develops sustainable business strategies and solutions through consulting, research and cross-sector collaboration.

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