

▶ SUPPLY
CHAIN
RISK

Pressure is growing on global corporates to tackle unacceptable labour practices in their supply chains, chiefly modern-day slavery

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If your supply chain is morally suspect, this is how you should react

No major corporate condones unethical labour practices. So why are firms still getting caught up in scandals at the more opaque ends of their supply chain?

In January, Apple, Sony and Samsung made headlines for all the wrong reasons. Human rights organisation Amnesty accused them and others of failing to ensure minerals in their products are not mined by children. Though all three have stated zero tolerance for child labour, the incident highlights the potential financial and reputational impact of unethical activities in a supply chain.

In the survey for this report, risk managers were asked how confident they were that their supply chain was acting ethically, on a scale of one (where unethical behaviour is non-existent) to five (where it is rife). The overall score was 3.44, indicating an above-average confidence in the supply chain, but with clear room for improvement.

One respondent said: “We engage a wide variety of suppliers, all with varying cultures, systems and values. While we have a comprehensive vendor assurance programme to mitigate risk, there is likely to be isolated incidents of unethical behaviour occurring.”

Cultural issues were highlighted too: “The organisation has set the tone from the top with a ‘zero tolerance’ on this issue. [But] the implementation of this policy defers between mature markets e.g. Hong Kong/Australia (which are intolerant to unethical practices) to China (where unethical practices seem to be an accepted norm).”

Lockton Singapore’s CEO, Peter Jackson, agrees there are problems with local regulatory body enforcement. But ignorance of wrongdoing is no excuse: “Your ultimate aim is to have visibility all the way down [the supply chain]. In the food industry, for example, it’s a ‘field to fork’ mentality.”

Control Risks associate director, global issues, Jonathan Wood, says supplier networks’ locations are also significant. “If you’re dealing with contract manufacturing in South East Asia, [the issues] might be human rights-related, but if you’re dealing with contract manufacturing in Europe, they might be product diversion and organised crime-related,” he



“EVEN AFTER TRAGEDIES LIKE THE FOXCONN SUICIDES OR THE COLLAPSE OF THE TEXTILE FACTORY IN BANGLADESH, THE TOLERANCE FOR SYSTEMIC CHILD LABOUR VIOLATIONS OR THE LACK OF A LIVING WAGE SUGGESTS THAT THE PRICE BEING PAID IS NOT HIGH ENOUGH.”

Managing partner,
RL Expert
Leesa Soulodre

adds. Approaching these issues “from a due diligence perspective and from a supplier chain auditing perspective are often quite similar skill sets”.

MILLIONS OF CHILDREN

The scale of unethical labour is huge, with 168 million children – almost 13% of youngsters globally – engaged in child labour, according to Unicef. In addition, modern slavery affects 36 million people, the Global Slavery Index estimates.

RL Expert managing partner Leesa Soulodre says multinationals have long profited from lax labour standards: “Even after tragedies like the Foxconn suicides or the collapse of the textile factory in Bangladesh, the tolerance for systemic child labour violations or the lack of a living wage suggests that the price being paid is not high enough, despite the reputation risks.”

But new regulation could see that change. The UK’s Modern Slavery Act 2015 is designed to consolidate previous offences relating to trafficking and slavery. The EU is said to be considering similar regulation.

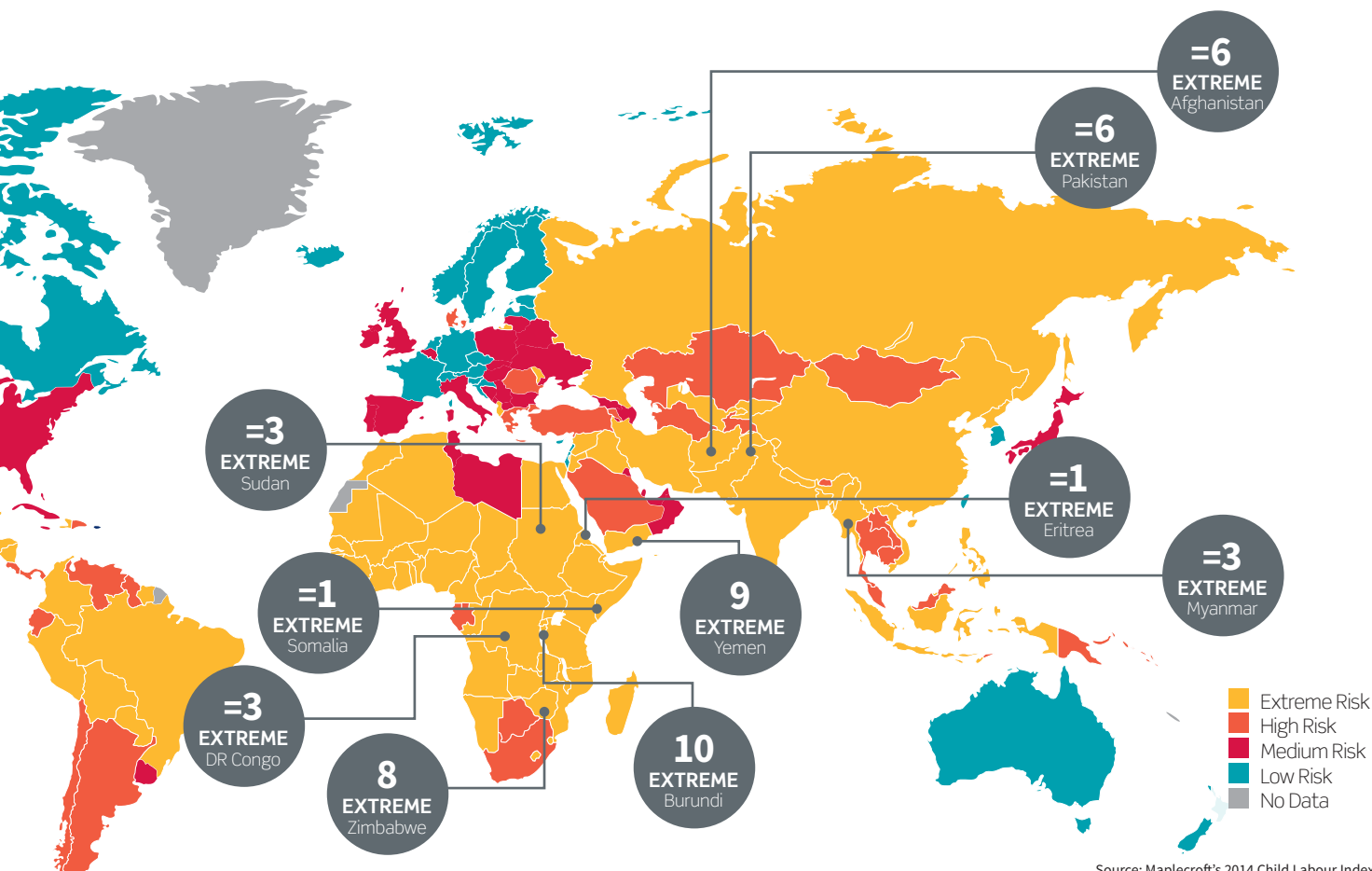
Soulodre wants to see “a collaborative process, with all stakeholders taking on responsibility. Company directors must demonstrate their fiduciary responsibility. “Companies can do this through ramping up their commitments and holding suppliers accountable to a set of standards.

“Governments need to enforce the law. NGOs must continue to be the watchdog, reporting company breaches of child labour to communities. Media need to responsibly report it. Employees need to be the whistleblower and vote with their employment choices, and workers, consumers and investors need to vote with their cash.”

Jackson agrees that firms should use their clout. He says: “Large customers can use the fact that they’re buying millions of dollars of materials to make people change because of the economic hulk grip that they have. Having said that, if that’s the stick, then there’s got to be a carrot as well to reward people for doing the right things.”

ABUSE OF CHILD WORKERS IS A GLOBAL ISSUE

Bangladesh, China, India, Nigeria and Pakistan are among 68 countries at an 'extreme risk'



THE ETHICAL ACTION PLAN

RL Expert Group managing partner Leesa Souldre

- 1 Implement an early warning system to increase transparency and monitor risks and issues in all tiers of the supply chain.
- 2 Get the chief executive onboard. Use them to help actively propagate an organisational culture around the importance of a responsible supply chain and corporate social responsibility (CSR) programme. Without this, it will clearly fail.
- 3 Ensure all staff are educated on the programme and understand the individual consequences of using a factory that has not gone through the CSR audit process prior to any orders being placed.
- 4 Zero tolerance of the use of child labour in all tiers of your supply chain should be clearly articulated as part of the signed supplier code of conduct and checks for breaches must form a critical part of the ongoing factory audit process by a specialised independent third party.
- 5 Factor 'outrage' into your assessment. Implement a rating system and rate the supplier inside-out, based on their audit result (what they told you) and what your stakeholders have published (what others say about them). Understand their sensitivity to this topic as gauged by your risk intelligence. For example, a 'red rating' could be assigned when any one of the audit requirements have not been met for critical risk issues and when stakeholder outrage is low. In this case, it would require a completed corrective action plan to be submitted within a short timeframe, with a follow-up visit within 30-60 days to evaluate remediation of issues.
- 6 Make sure a regular audit cycle forms part of the ongoing programme and records and results are maintained in a central place, easily accessible by frontline staff. Ensure outrage is factored into the hazard and probability risk assessment.

Stamping out the slave trade

Modern-day slavery affects millions – and if companies don't tackle it soon, governments and human rights activists are ready to punish them

About 45 million people live as modern-day slaves and 60% of those, or 27 million, are in Asia. This startling statistic from the anti-slavery, non-profit group Walk Free indicates the terrible scale of the issue.

And with 70% of global trade touching Asia in some way, according to Thomson Reuters, the issue of human rights in the supply chain should be on every risk manager's radar.

Over the past 12 months, growing investor pressure, media scrutiny and legislative requirements have seen companies place greater emphasis on the recruitment practices in their labour supply chains.

New legislation includes the UK Modern Slavery Act, the California Transparency in Supply Chains Act and the US Federal Acquisition Regulation.

Among other things, the UK's Act requires British firms – and any foreign company that has a subsidiary in the UK with a turnover of £36m or more – to state publicly that their supply chain is free of slavery.

In another move, a group of human rights activists and socially responsible investors are collecting data about the human rights efforts of 108 large companies around the globe.

The Corporate Human Rights Benchmark will then rank those businesses from best to worst. The goal is to make them follow through on pledges to avoid human trafficking, forced labour and other abuses.

All in all, this means that risk managers, especially those in Asia, should prepare for greater scrutiny of their supply chains, says Thomson Reuters head of risk Asia-Pacific, Kristen Tiner. "Unfortunately Asia is really one of the hotbeds for this type of behaviour and in particular, in certain industries like agriculture, fishing and mining," she says.

A question often asked is how far down a supply chain companies should go to ensure their supply chain is not morally suspect. Tiner says the trend in stable industries is two levels deep: your suppliers' suppliers. In industries with a higher exposure to human rights abuses, a deeper dive is required.



"ASIA IS ONE OF THE HOTBEDS FOR THIS TYPE OF BEHAVIOUR, PARTICULARLY IN AGRICULTURE, FISHING AND MINING"

Asia-Pacific head of risk,
Thomson Reuters
Kristen Tiner

"In the conflict minerals space, for example, you may have to go all the way back to the mine where it was sourced to prove that it didn't come from a conflict zone," she says.

Parsons Brinckerhoff Asia-Pacific global risk, ethics and compliance officer Adam Hing agrees it's difficult to determine. "We employ a risk-based approach and analyse how far down the supply chain we need go in terms of our due diligence based on criteria such as where in the world we are doing business, the goods or services involved and whether our supplier is a major one," he says.

As an engineering professional services firm, the risk of human rights issues in the company's supply chain is fairly low, says Hing. But managers are "acutely aware" that their supply chain must be carefully managed. "Most of our supply chain is external and we therefore have less control over it. To manage this, we ensure that we vet our suppliers prior to working with them. We also expect all of our suppliers to act in accordance with our 'five precepts of business ethics', which are contained in our third party code of conduct."

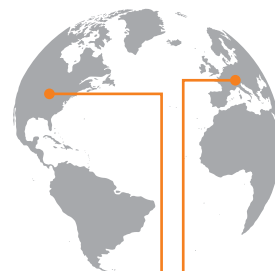
Hing adds that the risk of unethical labour in the supply chain is becoming a greater challenge for organisations to manage. "The global market is shrinking rapidly and relationships are becoming more remote and far less personal. That makes it extremely difficult for businesses to maintain a close relationship with every third party they deal with."

THE SCALE OF THE ISSUE



21m

21 million people are enslaved or in forced labour today*



1.5m

1.5 million of the victims are in Europe or North America

Source: The International Labor Organization (ILO) or http://www.leginfo.ca.gov/pub/09-10/bill/sen/sb_0651-0700/sb_657_bill_20100930_chaptered.pdf http://www.verite.org/sites/default/files/VTE_WhitePaper_

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THE IMPORTANCE OF KNOWING YOUR THIRD PARTY



WARRICK BEAVER

Managing director, customer and third party risk, Thomson Reuters

The impact of globalisation on supply chains now and in the future cannot be underestimated. Often what leads to mishaps is not the complexity of supply chains, but the lack of third-party management, transparency and monitoring which is fundamental from the beginning of the supply chain through to the end consumer.

Organisations that are aware of supply chain challenges and take proactive steps to address them will be well-positioned to ensure their supply chains serve existing customers more effectively, operate more efficiently, penetrate new markets and, overall, grow more profitably.

In today's business environment, organisations are increasingly being held responsible for the actions of their suppliers, vendors and partners, in addition to their own internal activities.

Pressure is intensifying for businesses to take proactive measures and responsibility for the conduct of their third parties and in their dealings with them. If third parties are held to a higher standard, this can reduce the probability of corruption, money laundering and tax evasion and other activities in the value chain. These activities are not only both morally and legally wrong, but also damaging to business and society.

By unwrapping the opaque and complex value chain between supplier and consumer or channel partner and broker, we are beginning to recognise that every component has to act in a compliant and responsible fashion for the system to operate optimally.

Through increasing demands for transparency, we are seeing the return of the voice in the customer in how and what they buy or consume and this is having a ripple effect through the value chain, including greater government participation.

By exposing, understanding and then monitoring the many nodes, connection points and related parties involved in a company's ecosystem, companies can take active measures to ensure that their business is secure and its operations are sustainable at a holistic and bilateral relationship level.

➤ For more information on exposing risks or opportunities within your supply chain, visit risk.thomsonreuters.com

A spokesperson from Allianz Global Corporate and Specialty notes: "While it is impractical for a company to audit and monitor each and every supplier in its entire supply chain at all levels, businesses should be able to manage their supply chain by working to identify key vulnerabilities and taking a risk management approach to ethical procurement."

Professional procurement can play a major role in driving unethical practices out of the supply chain, according to the spokesperson. "Procurement professionals have critical influence over, and visibility of, supply chain decision-making, especially over what level of due diligence is done, how suppliers and tenders are evaluated and assessed, and in establishing business systems to deal with risk."

Technology and data management can also help companies decrease the risk of being caught up in a human rights scandal and the potentially devastating reputational and financial impacts that come with it, says Tiner. She recommends companies look to automate as much of their supply chain management as possible. "The worst thing I think people can do is go and hire an army of people," she adds, pointing to the risk of human error and the long-term sustainability of this approach.

Instead, she advocates having a single system of record for every supplier. "It sounds basic, but most of this is being managed through separate spreadsheets or through procurement systems."

Tiner's second recommendation is to screen supplier information daily.

"We advocate a continuous and ongoing monitoring process so that, at any point in time, should something change – a new profile comes in, or there's a change to the status of an individual or company – you're automatically alerted to that the same day; you're not finding it out six months later and then exposing your business to that risk.

"Then for any good risk-managed vendor programme, you'd be looking at a certain refresh of vendors: how many do you have, are you looking to consolidate, do you understand, if a vendor fails, what the impact is on your business?"

She points out that the culture of an organisation plays a vital role. "It's important that it's not just the tone from the top, but that it is embedded into the life of the employees and that they buy in to that culturally," she says.

Key components include training programmes, bonuses for doing the right thing, and mechanisms to highlight good, as well as bad, behaviour.

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putting me in the
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