Are Supply Chains Truly Ready to Go “Beyond” Audits?

At AI, our extensive experience rolling out Supplier Audit Programs globally for some of the world’s largest brands and retailers has given us unique insights into how audits can help build better, more sustainable supply chains.
Supplier audits, one of the most widespread tools in managing ethical, social, and environmental compliance in global supply chains, have recently come under a barrage of criticisms. Some critics paint audits as toothless and inefficient, while others claim audits are actually detrimental to the ethical and environmental state of supply chains.

It is common to call for supply chain sustainability to go “beyond” audits. Depending on the context, this can mean replacing “boots on the ground” with high-tech solutions, introducing self-assessment tools, involving NGOs, conducting undercover investigations, and many other options.

Can these new methods and approaches, whether individually or in combination, fully replace supplier audits as a sustainability tool? This paper looks into the common challenges faced by supply chain ethics and compliance tools to explore a vital question: are supply chains truly ready to go “beyond” audits?

The Cornerstone of Compliance: Accurate Data

After years of collaborating with suppliers towards continuous improvement, many brands move towards introducing elements of self-assessment, as they strive towards one of the ultimate goals of supply chain sustainability: to have a network of responsible partners that need no policing and little external governance. Many mature CSR (Corporate Social Responsibility) systems are indeed ready to take supplier relations to this step. However, one cannot forget that today’s complex, multi-level compliance systems have been built on the foundation of field data gathered through factory audits.

Major brands recognize that accurate data is the cornerstone of any successful strategy to improve supply chain ethics, and usually rely on a combination of supplier audits and external sources (such as NGO reports) to inform their compliance efforts. For example, M&S, one of the UK’s largest retailers and a recognized sustainability leader, says that audits play an important role in assessing the management systems their suppliers have in place to mitigate human rights risks. Data gathered during regular factory audits is instrumental in identifying salient human rights issues, which, in turn, dictate the order of priority of corrective action and shape the brand’s risk management process vis-à-vis supply chain compliance.¹

Audits are not the only tool for data collection, and among the alternatives suggested by their critics, two options stand out in particular: an advanced technological approach, for example, risk mapping software; and direct investigation by NGOs and members of the press. Both have undeniable merits, yet neither is without limitation.

For risk mapping software, data quality remains a struggle, not least because inputs largely rely on suppliers’ self-assessments. Even with the best analysts cross-checking answers, there is no guarantee that all information provided by suppliers is error-free and, more importantly, truthful. Compliance management methods that rely on self-assessment are more suited for mature CSR systems, and even then they should not be used indiscriminately, but limited to those suppliers who had proven themselves as responsible, trustworthy, and committed to improvement.
Targeted investigations, especially those involving undercover work, can be effective in uncovering major human rights violations, as seen from the modern slavery scandals of the past few years, or the recent reports about the exploitation of Syrian refugees. That said, perception bias always plays a part: the findings of ‘successful’ investigations are widely publicized, while the rest remain unknown to the public. When the media are involved, sensationalizing can get in the way of contributing to supply chain improvement – or even in the way of the truth, as in the case of a 2008 BBC documentary that included fake footage, which the channel ended up publicly apologizing for. NGOs are more responsible in their reporting, but being independent, they traditionally pursue their own agenda, with little consideration to how constructive and helpful their initiatives are to the big picture of supply chain management. Finally, even if all independent parties act in good conscience and with the best of intentions, the scale of global manufacturing is incommensurate with their resources.

Ultimately, the massive scale of global supply chains dictates the choice of tools for improving compliance within them. Major brands and retailers work with hundreds of factories globally, and no external organization or media outlet has the resources to monitor them all. These days, more and more brands are recognizing their responsibility for their supply chain and take steps to improve it, especially in terms of human rights, safety, and environmental impact. Whatever a brand’s supply chain sustainability strategy, it must be able to reliably measure and assess the situation on-site, benchmark the results, and clearly identify areas for improvement. Only then, based on available data, can brands determine their next steps, such as educating and training suppliers, involving NGOs, or rolling out risk mapping programs.
For a brand, accurate supply chain data often starts at something as simple as knowing where their products are actually manufactured. In 2013, the Rana Plaza collapse shone a light on the scale of unauthorized subcontracting in the clothing industry. Three years later, surveys show that supply chain visibility still remains low: only 15% of brands have good visibility into their Tier 2 suppliers, and only 6%, into Tier 3.5

This lack of visibility is often blamed on audit methodology, but in reality, it is up to every brand to clearly set the scope of their auditing program. Take Patagonia, who made an executive decision to extend audits to their Tier 2 suppliers in Taiwan in 2011, and promptly discovered forced labor among the subcontractors. The brand openly announced their findings, and proceeded to continuously report on the steps taken to improve the state of human rights in their supply chain. That included ensuring restitution for affected workers, developing and implementing a new employment standard for migrant workers, and educating their suppliers.6

More recently, Apple uncovered bonded labor in their supply chain during 2016, with subcontractors among the main offenders. First-tier suppliers are also sometimes guilty of labor violations, but Apple reports that virtually all serious violations occur during a first assessment, and repeat violations are very rare. The brand paid a total of $2.6 million to over 1,000 supplier employees to cover cases of bonded labor.7

Patagonia’s and Apple’s examples show that even after working towards sustainability for years, brands can find themselves lacking accurate supply chain information. Despite cutting-edge technologies available to brands today, “boots on the ground” often remains the only way to investigate and map the reality of complex, multi-tiered structures that are modern global supply chains.

“Fire and Forget” Does Not Work

The state of global supply chains has been in the public eye in the past few years, and while public pressure created more incentives for brands to source more ethically and sustainably, the failures traditionally make for better media headlines. However, incremental progress is present in supply chain ethics, and so far, it has resulted not from one-time actions, but from consistency and regular follow-up. The goal of any supply chain compliance program is not simply improvement, but continuous improvement.

A look into the CSR reports of major brands shows what impact audit programs can have when applied consistently and over the long term. For example, suppliers to Adidas have shown a steady improvement in compliance scores over the years: the share of factories rated “good” for social compliance (3C or above on the brand’s own scale) has increased from 54% in 2013 to 69% in 2015, while the percentage of factories with severe non-compliances has dropped from 3% to 1% during the same time.8 In terms of environmental compliance, the improvement over the three-year period was from 55% to 81% “good” factories, and over 75% of suppliers would usually improve their environmental performance within one year of the initial audit.9 Adidas’ audit
coverage of contracted factories is 59% in countries considered high-risk for human rights issues (which includes most of traditional sourcing destinations in Asia). The trend observed by the company is that factories score low during their initial assessment, but improve over time with continued support and follow-up. Indeed, follow-up is crucial to progress, as one audit, even performed to perfection, will accomplish little in the long run. To effect lasting change, a brand needs to know which of its interventions are effective. That means conducting regular and recurring audits that monitor the implementation of Corrective Action Plans and closely track progress in all problematic areas. The frequency of recurring audits varies depending on the severity of situation and the extent of intervention, but annual re-audits are considered the accepted minimal standard.

Among the testimonies to the power of consistency are Apple’s continuing efforts to improve working conditions in its supply chain: in 2016, the company carried out 705 ethical audits of its suppliers (up from 640 in 2015 and 633 in 2014). Based on the collected data, the company conducts regular follow-up visits every 30, 60, and 90 days to ensure that working conditions are not compromised. In 2016, the number of suppliers complying with Apple’s working hours standard was 98%, an all-time high for the brand. Apple also successfully used environmental audits to slash emissions in its supply chains by over 150,000 metric tons, divert over 200,000 metric tons of waste from landfill in 2016, and save 3.8 bn gallons of water since 2013. Independent third-party audits are also used at all smelters and refiners of tin, tungsten, tantalum, gold, and cobalt, in a continuing effort to eliminate conflict minerals from Apple’s products.

Other examples of continuous improvement are Nike, whose audit program has resulted in an increase of compliant (“bronze”) factories from 70% to 86% in the past three years, and Target, who saw 1131 of its suppliers audited and remediated for labor and human rights issues in 2015. Target’s percentage of “acceptable” audit results ranged between 53% and 76% in 2015, depending on the region, with a global average of 64% – whereas a few years back, that number was below 50%.

That said, incremental progress does not mean inaction in the short term, especially when it comes to zero tolerance issues. Factory audits do have an immediate impact on the state of human rights in supply chains, as seen from the M&S Modern Slavery Statement 2015/16. Starting 2015, the UK’s Modern Slavery Act requires companies to publicly report on their efforts to eradicate forced labor from their supply chains. According to M&S’s first ever MSA statement, its ethical audits at factories identified 14 cases of non-compliance with the criteria “employment is freely chosen” (including lack of clear policy on forced labor, restriction of toilet breaks, deposit payments for protective equipment, and retention of workers’ passports). All instances have been followed up, through remedial action plans and cooperation with experts on the ground. M&S also declared their commitment to involve forced labor experts in their audits, in order to zero in on the problem with maximum effectiveness.

These examples, and countless others, show how effective audits can be when used properly: from immediate impact on the ground, to objective assessment of factories, to empowering improvement by providing brands with real data.
What Makes for a Meaningful Audit?

Ultimately, it is up to the brand to take action based on the audit findings. Nevertheless, there are several important criteria for ensuring that supplier audits provide brands with accurate information about the real state of ethics and social compliance in their supply chains.

INDEPENDENCE OF BRAND AND SUPPLIER.
Auditors on the brand’s payroll may be coerced by the management to doctor their findings, while those who have a vested interest in the supplier’s success may purposefully overlook violations. Using independent, or third-party, audit providers is the only way to prevent conflict of interest, and minimize the risk of fraud.

EFFECTIVE CHECKS AGAINST CORRUPTION.
Corruption risks exist even in case of third-party audits. It may happen that suppliers try to offer auditors bribes, gifts, or favors to persuade them to omit some of the more damning findings. To prevent and root out corruption, third-party auditing companies use a number of measures, from ethical training, to internal investigation and shadow audits, to financial incentives for reporting bribery attempts, combined with zero tolerance policies for corruption.

KNOWLEDGE OF MARKET, CULTURE, AND LANGUAGE.
Language and cultural barriers immediately limit the effectiveness of any audit, and may distort its findings. Cultural context is also very important when it comes to assessing the state of human rights, as workers’ backgrounds may affect their tolerance of the conditions they work in. Good auditors with local knowledge and experience know how to establish rapport with the factory management and floor staff and receive an accurate picture.

PUTTING WORKERS FIRST.
All too frequently, factory managers resort to deception and intimidation to cover up human rights violations. As a result, feedback given by workers at the factory may not reflect the real state of things. Because of this, it is extremely important that workers are provided with reporting channels that they can use safely, confidentially, and outside of their working hours – such as anonymous direct phone lines to auditors.

SEMI-ANNOUNCED OR SURPRISE AUDITS.
To minimize the chance of deception on the part of factories (e.g. sending underage workers home on the day of the audit), audits are best performed on a semi-announced basis, where factories are informed of an impending audit’s time frame, but never a specific day. In particularly high-risk situations, where there are grounds to suspect serious human rights violations and cover-up attempts, unannounced “surprise” audits may be performed.
A Strong Foundation for Lasting Improvement

So, are supply chains ready to go “beyond” audits? As in any complex issue, there can be no one-size-fits-all answer. Brands with mature CSR systems may be sufficiently equipped to go “beyond” audits and work on continuous improvement – but the way to those mature CSR systems is paved by years of comprehensive audit programs and consistent follow-up. For many brands, that stage is still a long way down the road: data collected by AI from over a thousand ethical audits conducted in 2016 shows that only 36% of factories were found compliant, while 27% had critical non-compliances, and the rest were in need of improvement.

Today, all participants of supply chains understand that supply chain compliance is a global, incredibly complex issue, and no one entity can tackle it single-handedly. Instead of trying to go it alone, brands, governments, and NGOs are encouraged to cooperate in order to create lasting changes. When it comes to compliance tools, the situation is similar. No single compliance tool or method is all-encompassing and sufficient on its own – this may very well be the one thing all supply chain professionals agree on.

Creating improvement in the long term requires a comprehensive and adaptable strategy, with an arsenal of tools and a strong foundation of reliable data. **Being an invaluable, often irreplaceable source of real supply chain data, supplier audits form an integral part of that foundation.**

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About AsiaInspection

AI is a global leading quality control and compliance service provider that partners with brands, retailers and importers around the world to secure, manage, and optimize their supply chain.

AI performs Supplier Audits Programs, Product Inspections, and Laboratory Testing. Clients from over 120 countries worldwide benefit from web-based mobile friendly account management, fast scheduling, and highly competitive all-inclusive pricing: $309 for Product Inspections and $649 for Factory Audits.

AI guarantees on-site arrival within 48 hours of booking, and a same-day inspection report available online.

With over 1,500 inspectors and auditors classified by product range and auditing expertise, account managers speaking over 20 languages, and service coverage of 85 countries, AsiaInspection is Your Eyes in the Supply Chain™.
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