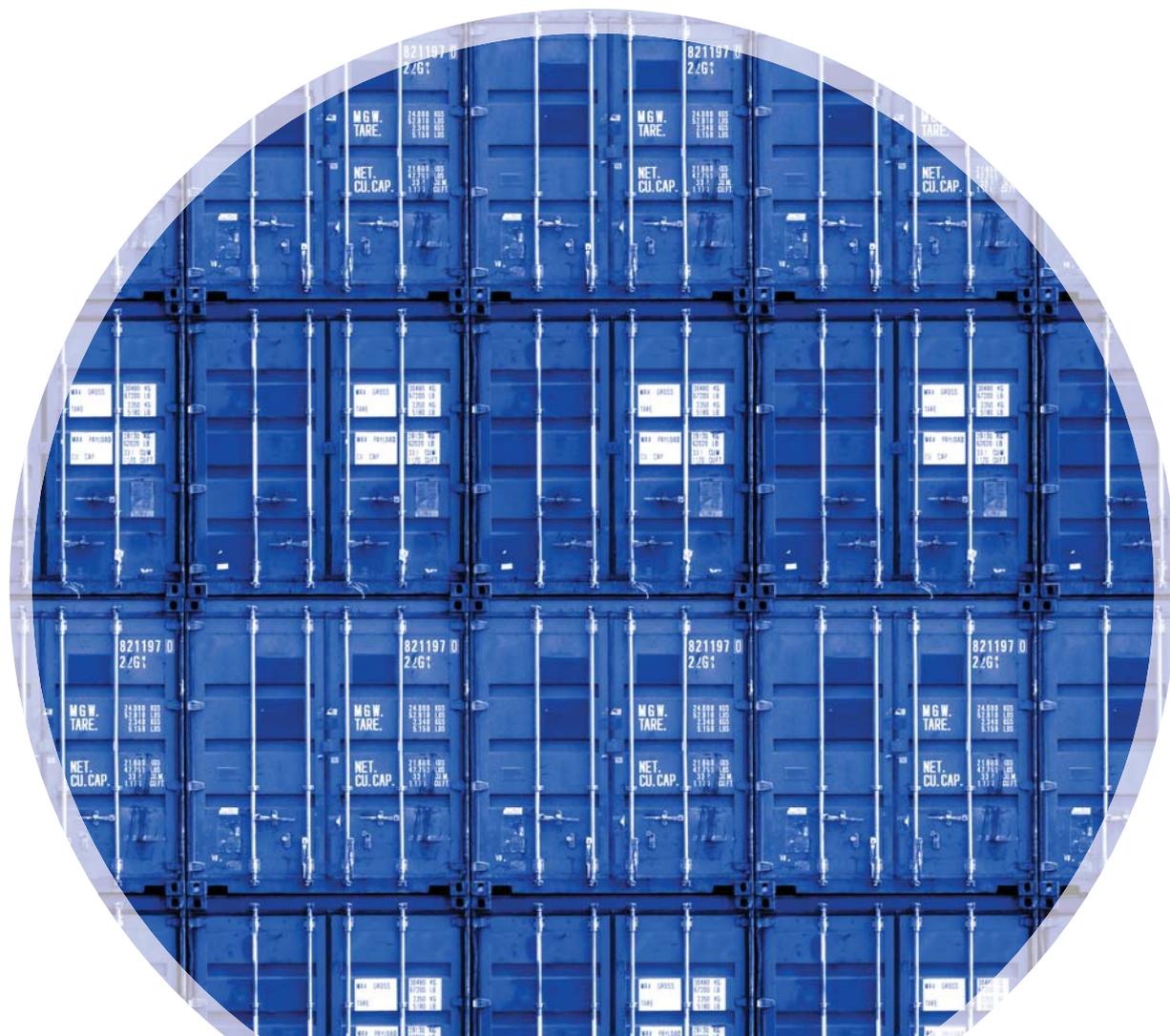


# Responsible Supply Chain Management

Where do companies stand?







# PREFACE

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Globalisation has enabled companies and markets to multiply the volumes, the speed, and the profitability of their operations in unprecedented proportions. However, it also triggers skepticism and critics. The internationalisation of supply chains is both the backbone and the dynamo of globalisation. It has important social consequences and environmental impacts, ultimately influencing its image and acceptability in public opinion and among civil society.

Globalisation could be a real opportunity for social progress if international supply chains and chains of production were oriented from the top towards the implementation of principles of action as defined by international labour law, and human rights and the environment. On the contrary, the support towards globalisation might be dangerously weakened, as well as for democracy and the global economy, if international supply chains were only to be influenced by the lowest standards of social and environmental practices.

It is in this spirit that, after its Summit in June 2015, the G7 emphasised the links between international corporate supply chains and the application of social and environmental norms recognising *“the joint responsibility of governments and businesses to foster sustainable supply chains”*. This commitment is in line with the intergovernmental dynamics, which can seem slow and hesitating, but is real and imposes on companies their own responsibility to comply with human rights, particularly environmental norms and the fundamental social rights in the workplace. On this point, a major milestone was achieved with the approval of a framework for the

implementation of “Guiding Principles on Business and Human Rights” on June 16th 2011 by the United Nations Human Rights Council. Companies’ responsibility to respect human rights must apply to their direct activities and their spheres of influence. This incorporates a companies’ purchasing activities with their external suppliers, as well as internal procurement operations with their international network of subsidiaries and subcontractors.

This study is based on Equitics©, our exclusive methodology of analysis and rating.

With this study Vigeo Eiris evaluates the degree to which listed companies around the globe report on the respect of international social and environmental norms in their supply chain management. The outcomes are disappointing. Only a minority of companies are able to demonstrate a responsible management of their supply chain. In parallel to this aspect, very few of them are directly facing controversies on their behaviour regarding international supply and procurement. Among the 38 sustainability drivers on which Vigeo analyses the social responsibility risks and behaviours of companies, the integration of social and environmental standards in the supply chain is one of the drivers on which listed companies provide the least amount of information, are the least performant and are least subject to controversies.

While at the global scale more than one listed company over five faces allegations on corruption, very few are subject to controversies for having neglected or not complied with social norms in their international activities. Only 2.2% of them are facing allegations regarding their environmental

[1] See the debate held in France on the draft bill for parent companies’ “Duty of Vigilance”. (<http://www.senat.fr/dossier-legislatif/pp14-376.html#timeline-10>)

behaviour. Although these figures seem to suggest that social and environmental supply chain issues remain marginal among the social responsibility drivers raised by stakeholders, the cases illustrated in this study demonstrate significant legal implications. The debate held in France on the companies' due diligence towards their subsidiaries' behaviour – although the issue is still legally evolving – confirms that it is a risk area that companies should remain attentive to. This study shows that for some sectors such as retail, supermarket, food and beverage, luxury, cosmetics, or energy, the controversies on the subject of procurement and management of international supply chain have already reached the alert level.

This study also highlights the most convincing managerial behaviours. They first consist in defining principles and making them visible without employing ambiguous terms on the companies' will to prevent any form of social or environmental dumping or to comply with the principles and dispositions of international norms, such as those of the International Labor Organization, as well as the objectives of important International Agreements for environmental protection. Companies indicate the precise names and references of the international conventions' principles and goals that they commit to observe, even if these instruments are initially intended for

States.

Companies integrating a social responsibility approach into their supply chain and procurement processes explicitly indicate the social and environmental criteria on which they select and evaluate their suppliers and subcontractors. They report on the intelligibility and the proportionate nature of the clauses from which they transpose their social responsibility commitments into their purchasing contracts. For them to be able to capture a reasonable assurance on their validity and consistency, these commitments need to be backed by enhanced accountability on the means allocated to them, the controls that they are subject to, and the corrective measures resulting from them. They should also indicate in the most accurate way the social and environmental standards used and their evaluation frameworks.

However, the supply chain's monitoring must not simply stay defensive by aiming to prevent the risks of violating social and environmental norms. Customers' and buyers' social responsibility is also a positive responsibility that should lead to the subcontractors' progress on social and environmental aspects, and should contribute to human development in their operating territories. In this regard, it is essential to report on the social and environmental nature and impacts of the corrective measures obtained from the assessment of procurement and supply chain processes.

## KEY FINDINGS

### OBJECTIVES OF THIS STUDY:

- To present and examine the current status of responsible supply chain management reported by companies across a wide range of industries and regions;
- To highlight the controversies faced by companies and their responses, particularly in sectors highly exposed to allegations;
- To highlight best practices, in order to recognise specific company performances, as well as to identify actions that companies can take to work towards more efficient responsible supply chain management.

- Despite mediatisation and emotive events, such as the Rana Plaza collapse, the average performance towards responsible supply chain management remains weak.
- The above trend is true for all regions and all countries. This indicates that although we live in a world with globalised production and consumption, we continue to see a very segmented world in terms of environmental and social standards.
- This phenomenon is receiving wider media coverage. However, relatively few companies actually face direct supply chain allegations (less than 7% of companies). This indicates that supply chain management remains a marginal topic in the CSR and consumer arena.
- Although there are some best practices, overall there is a lack of evidence that companies are engaging with stakeholders (such as NGOs and trade unions) to avoid environmental and social dumping, or to enhance global standards across value chains (around 3% of companies report this engagement).
- Companies appear to focus more on selecting and controlling suppliers on social and environmental standards, than on developing fair and balanced relations with suppliers. Indeed, approximately 30% of companies examined do not report on any commitments and measures to address the latter.
- Around a third of companies do report to have implemented audits. However, there is a lack of assurance on the topics covered by these audits, on the independence of auditors and on the systematic follow up if incidents are identified.
- Overall, companies report more on policies and commitments to integrating social and environmental factors into their supply chains and to ensuring sustainable relations with suppliers, rather than on actual measures that have been put in place (such as audits, training, questionnaires, risk mapping). Amongst the companies that do report on the measure in place, there is very low assurance provided that these measures are implemented throughout companies' supply chains (less than 3% of companies report this).
- The vast majority of companies do not report that they have implemented corrective measures for any social or environmental incidents identified in their supply chains. This is a concern because a lack of follow up can completely undermine the utility of audits and any other measures installed.



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### STUDY UNIVERSE:

- The evaluated sample includes companies that are headquartered or listed in **European, North American (United States, Canada) and the Asia Pacific**
- These companies were assessed by Vigeo between **May 2013 and May 2015**
- **1288 companies** assessed on the integration of social and environmental factors into their supply chains.\*
- **181 companies** assessed on the sustainable relations with suppliers (companies in Food, Beverage, Tobacco, Specialised Retail and Supermarkets sectors).\*

*\*The percentages indicated in the study are based on our evaluated sample*

## ● Context

*“Unsafe and poor working conditions lead to significant social and economic losses and are linked to environmental damage. Given our prominent share in the globalization process, G7 countries have an important role to play in promoting labour rights, decent working conditions and environmental protection in global supply chains.*

***We will strive for better application of internationally recognized labour, social and environmental standards, principles and commitments (in particular UN, OECD, ILO and applicable environmental agreements) in global supply chains. We will engage with other countries, for example within the G20, to that end.***

*We strongly support the UN Guiding Principles on Business and Human Rights and welcome the efforts to set up substantive National Action Plans. In line with the UN Guiding Principles, we urge private sector implementation of human rights due diligence. We will take action to promote better working conditions by increasing transparency, promoting identification and prevention of risks and strengthening complaint mechanisms.*

***We recognize the joint responsibility of governments and business to foster sustainable supply chains and encourage best practices.”***

Leaders' Declaration G7 Summit'  
7-8 June 2015

## ● Key supply chain trends

- The acceleration of globalisation is mainly driven by companies outsourcing production processes to a larger and larger web of suppliers and by the relocated of production sites. Through this process there have been substantial cost reductions and gains for businesses. However, this has led to more and more threats to **social and environmental dumping**. For example, impacting health and safety standards and the upholding of fundamental human rights (such as freedom of association, collective bargaining and non-discrimination).
- As part of this outsourcing process, the **complexity** of supply chains has increased, not only in terms of regional distribution, but also in terms of the number of different players.
- Despite or even given this complexity, companies are expected to manage their supply chains in order to avoid environmental and social dumping. According to the updated OECD

Guidelines for Multinational Enterprises (2011), paragraph 12 states that businesses should “Seek to prevent or mitigate an adverse impact where they have not contributed to that impact, when the impact is nevertheless directly linked to their operations, products or services by a business relationship”...“Where enterprises have large numbers of suppliers, they are encouraged to identify general areas where the risk of adverse impacts is most significant and, based on this risk assessment, prioritize suppliers for due diligence. In the context of its supply chain, if the enterprise identifies a risk of causing an adverse impact, then it should take the necessary steps to cease or prevent that impact”.

- Since these 2011 Guidelines, there have been key developments on clarifying **the meaning of conducting “due diligence”**. In particular, the “OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-

Affected and High-Risk Areas” (amended in 2012) and a similar guidance currently being developed for the Garment and Footwear Sector, gives companies practical guidance on how, when and by whom these principles should be implemented.

- There have also been a number of voluntary best practice initiatives, such as the Global Social Compliance Programme (GSCP), whose mission is to “harmonise existing efforts and deliver a common, consistent and global approach across sectors for the continuous improvement of working and environmental conditions in global supply chains”. This is a business-driven programme open to buying companies (brands and retailers) across all sectors and geographies. The GSCP has developed a set of tools and processes for companies to support companies’ in their implementation of social and environmental requirements in their supply chains.
- **Investors** are becoming more active players in influencing company behaviour on supply chain management<sup>(1)</sup>. To date, international approaches, as enshrined in self-regulation such as UN Principles for Responsible Investment, have urged investors to take a more stringent view of Responsible Investment.
- In the context of highly mediatised recent tragedies, such as the Rana Plaza collapse and the Thai prawn slavery scandal, there continue to be many questions raised on whether **traditional supply chain measures**, such as audits, are efficient tools to prevent supply chain disruptions and to prevent environmental and social dumping.

<sup>(1)</sup> *Global Social Compliance Programme – accessed 02/03/2016 – <http://supply-chain.unglobalcompact.org/site/article/126>*

<sup>(2)</sup> *For example, Norwegian Pension Fund – Company Exclusions – <https://www.regjeringen.no/en/topics/the-economy/the-government-pension-fund/internt-bruk/companies-excluded-from-the-investment-u/id447122/>*

## ● Key issues et principles of action

### ●● Key issues

- Through their procurement process, companies are increasingly facing reputational, legal and operational risks if they are considered to be involved in allegations, controversies or human catastrophes.

### SECTOR EXPOSURE EXAMPLES

- **Bargaining Power:** Technology Hardware and Telecommunications are part of the same value chain and therefore have communal dependency on the raw materials and workforces to make their products. However, due to their position in the value chain they have different leverage over the supply chain. Technology Hardware companies have an overall strong leverage to influence suppliers, due to their relative size (larger companies than their suppliers) and the choice of suppliers. This diffusion of risk over many companies allows the company to keep the bargaining power of any supplier to a minimum. The suppliers can therefore be pushed by these larger corporations to follow their demands, including addressing the social and environmental impact (which are particularly significant for rare earth elements). In turn, these hardware companies are the major suppliers to the Telecommunications companies, which therefore have lower capacity to influence their supply chain as they have less purchasing power and lower choice of supplier.
- **Level of Outsourcing:** In the apparel industry and textile sector, a large number of sporting goods and retail companies have fully outsourced manufacturing, while most high-end luxury good brands, especially jewellery and watch makers, keep the majority of manufacturing in-house. The latter are more likely to have knowledge and control over their production processes.

### ●● Principles of action

#### VIGEO EIRIS ASSESSES THE WAY THROUGH WHICH COMPANIES MITIGATE THESE RISKS THROUGH THREE DOMAINS OF RESPONSIBLE SUPPLY CHAIN MANAGEMENT

##### SUSTAINABLE RELATIONS WITH SUPPLIERS

Define and respect clear and reasonable contractual clauses

Engage and cooperate with suppliers

Build partnerships

##### INTEGRATION OF SOCIAL FACTORS

Monitor the social performance of suppliers and contractors

Promote the continuous improvement of suppliers' social performance

##### INTEGRATION OF ENVIRONMENTAL FACTORS

Monitor the environmental performance of suppliers and contractors

Promote the continuous improvement of suppliers' environmental performance

# INTEGRATION OF SOCIAL AND ENVIRONMENTAL FACTORS IN SUPPLY CHAIN MANAGEMENT

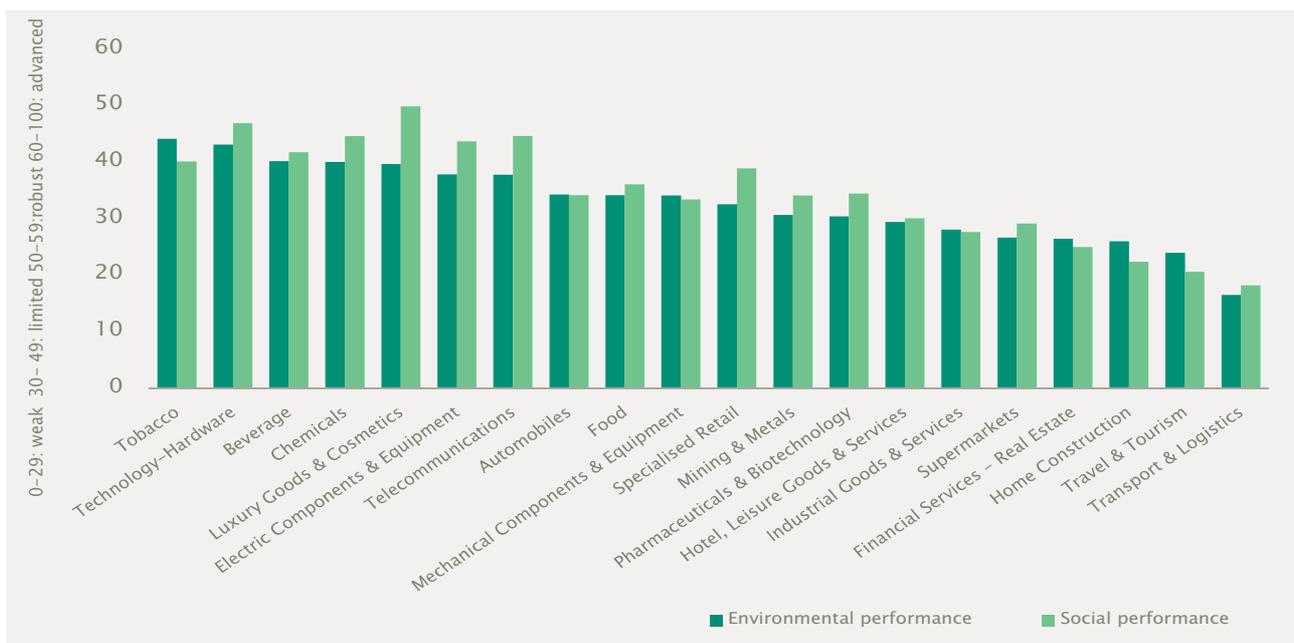
## OVERVIEW OF SECTOR, REGIONAL AND COMPANY PERFORMANCES

### ● How does sector activity influence companies' behaviour?

#### KEY FINDINGS<sup>(3)</sup>:

- Sectors facing both social and environmental issues in their supply chain demonstrate on average weak (less than 30/100) to limited performances (less than 50/100).
- Thus, despite differences in sector exposure to environmental and social supply chain challenges, there is **low heterogeneity between sector average performances**.
- Social and environmental factors appear to be rather equally tackled by sectors.
- Some sectors that are highly exposed to environmental and social challenges in their supply chains, such as Supermarkets, Real Estate, Travel & Tourism and Transport & Logistics, are nonetheless amongst those that appear the least committed to integrating both social and environmental issues in their supply chain.

#### ●● SECTOR PERFORMANCES ON INTEGRATING SOCIAL AND ENVIRONMENTAL FACTORS INTO SUPPLY CHAINS



<sup>(3)</sup> This graph only consider sectors exposed to both environmental and social issues in the supply chain (20 sectors). It presents the average score of companies in three regions, European, North America and Asia Pacific.

## SECTOR LEADERS

- The **Luxury Goods and Cosmetics sector** is the leading sector in terms of **integrating social issues in the supply chain** achieving a robust average score (50/100). This is a diverse, but highly exposed sector. For instance, in the cosmetic sub-sector, workers are exposed to harmful chemicals and in the pure luxury sub-sector companies are exposed to concerns of using conflict minerals (such as the extraction of diamonds from zones prone to human rights violations) and evidence of child labour (such as in the leather industry in Pakistan). However, the companies in this sector also often have a strong capacity to demand high standards from their suppliers. This is because normally the number of suppliers as well as the number of buying companies operating in these industries are relatively few (especially when compared to the textile and agricultural industries). This creates an environment in which companies can have more knowledge and even direct influence on suppliers.
- The **Tobacco sector** is the relative best performer regarding the managerial approach towards **integrating environmental standards of its supply chains**. However it should be noted that this average performance remains limited in absolute terms (44/100). Poor environmental management of tobacco crops can lead to excessive soil degradation and deforestation, which will ultimately prevent tobacco crops from growing. Companies can therefore promote sustainable tobacco cultivation and biodiversity protection to minimise future operational risks and preserve their own market capacity to produce and sell goods in the long term. The relative strength of this sector would suggest that overall these risks have been recognised and companies are taking at least some steps to manage them. This is also a sector that is highly scrutinised due to the impact of its products on human health, thus by reporting on its approach to supply chain management these companies' may be seizing opportunities to counter their negative reputation.

## SECTOR LAGGARDS

- According to a survey carried out by Consumer International, the world federation of consumer groups, an estimated 110 purchasing managers are employed by **supermarket** chains in Europe to act as intermediaries between 3.2 million farmers and 160 million consumers<sup>(4)</sup>. These intermediaries frequently exert strong pressure on suppliers to deliver goods and services at the lowest price and in the shortest time possible, which leads to the risk being 'externalised' and passed down the supply chain. 'Squeezing' suppliers in this way makes it increasingly difficult for the supplier to meet demanding orders while maintaining good working conditions and decent pay for workers. One major problem identified in the supermarkets' supply chain is the poor working conditions of migrant workers. For example, the Economical Council for Corporate Responsibility (ECCR), a Church-based investor coalition, found evidence of exploitation of migrant workers in British supermarkets' supply chains. In addition, the Equality and Human Rights Commission (EHRC) found significant evidence of abuse among producers, particularly from meat processing factories supplying Britain's big supermarkets. Despite such critical exposure, Vigeo has found that 40% of the supermarkets assessed still fail to disclose information on the kind of measures that are implemented to safeguard the environmental and social standards in their supply chains.
- When looking to **Transport & Logistics**, a sector that is highly exposed since most of its suppliers employ a blue collar workforce in physically-demanding working conditions, it is worth noting that 46% of the companies fail to disclose a commitment and this percentage raises to 68% when it comes down to allocating measures.
- Similarly, in the **Travel & Tourism** sectors a large majority of the companies fail to disclose information on the integration of social issues in their supply chain (51% do not report commitments and 61% do not report measures). This is a sector increasingly exposed to environmental and social

<sup>(4)</sup> This is according to an article published in the *Global Geopolitics & Political Economy* in April 2010

challenges in their supply chains, particularly due to the rapid increase in the range and number of suppliers contracts services (such as catering, fuelling and other related services).

- The **Real Estate** sector is highly exposed to social risks in the supply chain as it is increasingly outsourcing and using temporary agency work, whereby most of the activities are now usually carried out by external parties (such as contractors, home construction companies, property

managers, security, cleaners and other services providers). These suppliers often employ blue collar workers in physically-demanding working conditions, with challenges being found in ensuring health and safety protection and avoiding precarious contracts. Despite these challenges, 57% of the companies in this sector fail to disclose a commitment to integrate social standards in the supply chain, while only 35% report one or more measures being implemented.

## ● How does the location of companies' headquarters influence their behaviour?

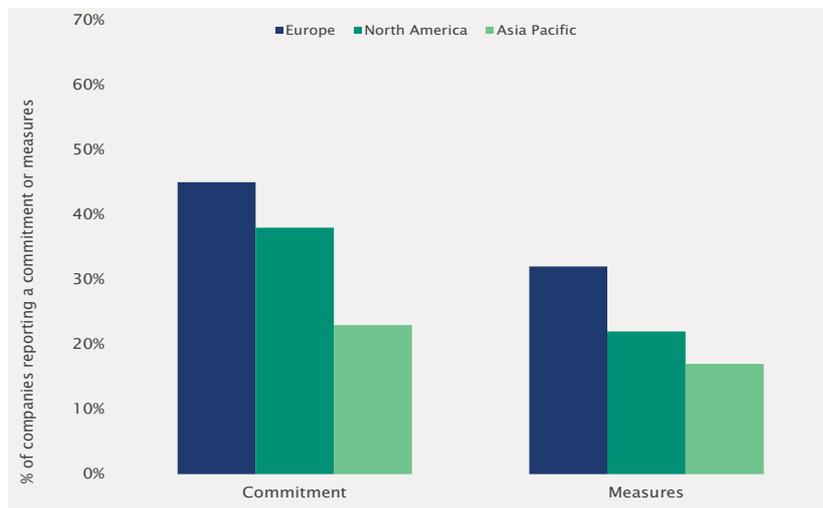
### KEY FINDINGS<sup>(5)</sup>

- Overall weak to limited average performances are obtained across the three regions (European, North American, Asia Pacific).

More than two thirds of companies do not disclose any kind of commitment to integrate social or environmental standards in their supply

chains. Around 40% fail to disclose information on any related measures. Very little assurance is provided that the reported measures are implemented throughout companies' whole supply chain (2.3% of the companies provide evidence that all main direct and indirect suppliers are covered by the reported measures).

### ● REGIONAL PERFORMANCES ON INTEGRATING SOCIAL AND ENVIRONMENTAL FACTORS INTO SUPPLY CHAINS



- However, there are regional differences. On average companies listed in Europe continue to lead, followed by companies in North America and then Asia Pacific. Worldwide, regulation on social and environmental standards in the supply chain remain limited and consumer pressure still appears to be weak. Regulation is more advanced in Europe and is emerging in North America (for example, EU Flegt Law 2010; US Dodd Frank Act 2010; California Transparency in Supply Chains Act 2010; UK Modern Slavery Act 2015<sup>(6)</sup>).

## EXAMINING REGIONAL DIFFERENCES

A reason for the slightly better European performance is the regulatory environment, both on a national and European-wide level. Throughout these supply chain regulations and initiatives there are two threads, disclosure and due diligence, both of which require companies to have increased knowledge about their supply chain and the origin of products and services. These European requirements are very much in line with recent developments in international soft law requirements, such as the revised OECD guidelines on multinational enterprises and the UN guiding principles on business and human rights.

For instance:

- In 2014, Europe adopted a directive on the disclosure\* of non-financial and diversity information (\*"Directive 014/95/EU" – accessed 05/01/2016 –www.eur-lex.europa.eu) by large companies and groups. The companies concerned must disclose information on policies, risks and outcomes with regards to environmental matters, social and employee-related aspects, respect for human rights, anti-corruption and bribery issues, and diversity on boards of directors;

<sup>(5)</sup> The notion of 'region' is determined by the country where the company is listed or headquartered, thus the analysis does not assess the locations of a company's operational presence/ supply chains.

<sup>(6)</sup> See next pages for more details on these regulations

<sup>(7)</sup> "EU Regulation on conflict minerals: What the European Parliament vote means for member states" – Amnesty International & Global Witness – June 2015 – p1

- In May 2015, the **European Parliament** voted in favour of a strong and binding law that requires companies trading in or using conflict minerals in their products to source responsibly. This new initiative went past the voluntary proposal made by the European Commission in March 2014, which was described as weak in a joint statement sent to the European Commission, the European Parliament, and the European Council, by a number of global sustainable and responsible investors and investment organisations<sup>(7)</sup>.
- **The EU Flegt Law**, adopted in October 2010, prohibits marketing of illegally logged timber on European markets and requires companies to exercise due diligence to minimise the risk that illegal products reach the market. The due diligence obligation requires companies to seek information about the origin of the timber, harvest conditions, suppliers involved, and compliance with national laws; to conduct a risk assessment; and to put in place mitigation measures. The law applies to virtually all paper-based products except recycled products and printed products such as books and magazines;
- **A bill has been submitted in France in March 2015**, obliging parent companies with more than 5000 employees present in this country to establish and implement a precautionary plan. This plan must identify, prevent and alleviate the risk of violations of human rights and fundamental freedoms in the supply chain. This bill is awaiting its last passage through the French Senate, having been adopted at the National Assembly's second reading. This bill is supported by trade unions and NGOs, but is facing opposition and criticism from companies.
- In March 2015, the UK adopted its **Modern Slavery Act**. This means that any business – or part of a business – that has a global turnover of GBP36m or more and supplies goods or services in the UK will have to produce and publish an annual slavery and trafficking statement in a “prominent” place on its website every year. The statement must set out what steps the organisation has taken to ensure there is no slavery in any part of its business, including its supply chains. This came into force in October 2015 and the reporting obligation will only apply to financial years starting on or after the 1st of April 2016<sup>(9)</sup>.

Although these factors are certainly influencing the European market, it must be highlighted that there are also **regulatory developments in North America**, which are pushing companies to report on steps taken to manage social and environmental supply chain challenges.

For example:

- With the adoption of the **US Dodd-Frank Act** in 2010, companies not only have to disclose whether the minerals (defined as gold, tin, tungsten, and tantalum) in their products originate from the Democratic Republic of Congo or neighbouring countries, but also report on the due diligence exercised when they do. This regulation applies to all companies listed in the US.
- The 2010 **California Transparency in Supply Chains Act** requires manufacturers and retailers doing business in this state<sup>(10)</sup> to disclose their policies, processes, and controls to eradicate slavery and human trafficking. Companies must provide consumers direct access to their disclosure from the homepage of their corporate websites.

<sup>(8)</sup> *Entreprises : le devoir de vigilance finira par s'imposer* – Le Monde Economie – 26/03/2015 ; *'Le big data mesure aussi l'empreinte sociale des entreprises'* – Le Monde Éco et entreprise – 10/02/2016

<sup>(9)</sup> *"Modern Slavery Act 2015"* – assessed February 2016 – <http://www.legislation.gov.uk>

<sup>(10)</sup> *This includes companies that meets any of the following four conditions : (1) The company is organized or commercially domiciled in California. (2) Sales in California for the applicable tax year exceed the lesser of \$500,000 or 25 percent of the company's total sales. (3)The value of the real and tangible personal property of a company in California exceeds the lesser of USD 50,000 or 25 percent of the company's total real and tangible personal property. (4) The amounts paid by a company in California for compensation exceeds the lesser of USD 50,000 or 25 percent of the total compensation paid by the company."*

- Alongside these development, stakeholders in the US are attempting to hold companies accountable for alleged human rights abuses in foreign countries under the **US Alien Tort Claims Act**. Since 1980, courts have interpreted this statute to allow foreign citizens to seek remedies in U.S. courts for human rights violations committed outside the United States. For example, **Nestlé**, **Cargill** and **Archer Daniels** are currently involved in a lawsuit regarding alleged child trafficking and forced labour. This case was launched in 2005 by two human rights organizations, Global Exchange and the International Labour Rights Fund. The plaintiffs accuse the companies of benefiting from child slave labour at cocoa bean plantations in Cote d'Ivoire. In September 2010, a court dismissed the case finding that the case could not be brought under the Alien Tort Claims Act. However, the plaintiffs appealed the dismissal and in December 2013, a federal appeals court overturned the 2010 ruling and allowed the plaintiffs to refile the lawsuit. In January 2016, the U.S. Supreme Court refused the dismissal of charges against three companies This case is therefore ongoing<sup>(1)</sup>.
- In the **Asia Pacific** region it appears that companies are under far less intense public scrutiny of social and environmental supply chain challenges or face regulation with regards to managing this issue. 47% of Asia pacific companies fail to disclose a dedicated supplier policy on social standards in the supply chain. Of the remaining 53% that do disclose policies, only 13% of the companies report to have a dedicated department responsible for implementing the commitment or provide evidence that local managers are held accountable. 41% of the companies listed in that region are not transparent on the kind of measures they adopt to protect social standards in the supply chain. When assessing performances on environmental standards, we notice slightly better performances. 67% of companies based in that region disclose commitments, of which 18% have a dedicated department responsible for the implementation of the policy. However, half of the companies fail to report on measures. This suggests that despite major supply chain challenges there still appears to be much room for improvement in the corporate managerial approach in this region.

<sup>(1)</sup> "U.S. Supreme Court gives boost to child slave labor case against Nestle" – Reuters – 13/01/16; – "Nestle Faces Lawsuit over Child Slavery in Ivory Coast" – Telesur – 12/01/16

## ● Top 20 Company performances on integrating environmental factors into supply chains

Title	Country	Sector	Sustainability Driver Score (/100)	Overall CSR Score (/100)	Market Cap (EUR bn)
Koninklijke DSM	Netherlands	Chemicals	88	63	9.666
Kimberly-Clark	USA	Luxury Goods & Cosmetics	87	55	34.683
Glencore	UK	Mining & Metals	83	58	50.873
Inditex	Spain	Specialised Retail	81	52	915
Danone	France	Food	78	64	39.450
Deutsche Telekom	Germany	Telecommunications	75	48	70.823
BT Group PLC	UK	Telecommunications	75	66	5.138
Lenovo Group Ltd.	Hong Kong	Technology-Hardware	73	39	1.451
NTT DoCoMo Inc.	Japan	Telecommunications	73	47	64.791
NEC Corp.	Japan	Technology-Hardware	73	50	7.270
Nestlé	Switzerland	Food	72	60	215.061
Novo Nordisk A/S	Denmark	Pharmaceuticals & Biotechnology	72	53	132.905
British Land Company	UK	Financial Services – Real Estate	72	67	11.812
Symrise AG	Germany	Chemicals	72	60	7.340
Schneider Electric	France	Electric Components & Equipment	72	56	372
Orange	France	Telecommunications	71	58	4.103
SKF	Sweden	Mechanical Components & Equipment	71	56	9.642
Sigma-Aldrich Corp.	USA	Chemicals	71	51	1.656
Telecom Italia	Italy	Telecommunications	70	51	21.115
Toshiba Corp.	Japan	Technology-Hardware	70	52	1.496

### KEY FINDINGS

- The top 20 companies all achieve advanced performance, ranging from 70/100 to 88/100.
- The top 20 companies are diverse in terms of their size, sector activities (11 different sectors) and regional representation (representation from North America, Asia Pacific and Europe). However, the majority are European.
- The most represented sectors are Technology Hardware and Telecommunications (making up 40% of the companies).
- Some of the most advanced companies belong to sectors that are highly exposed to the risks of environmental controversies in their supply chains.

### BEST PRACTICES ON INTEGRATING ENVIRONMENTAL FACTORS IN THE SUPPLY CHAIN

**Koninklijke DSM** is considered to be the leader on integrating environmental factors into the supply chain (score of 88/100):

- This company is part of the chemicals industry, an industry that transforms energy and raw materials into products required by other industrial sectors as well as by final consumers. The main suppliers of the chemicals industry can have a considerable impact on the environment (including on soils, surface water, ground water and ecosystems). All this accounts for the sector being under increasing NGO, investors and governments' scrutiny for respecting environmental standards in this supply chain.
- Koninklijke DSM has set quantitative targets (aims to work with suppliers to reduce their carbon footprint by 20% by 2020 using 2010 as reference). The company also reports a dedicated

structure responsible for this issue commitment, including evidence of comprehensive measures, including supplier training modules, integration of environmental clauses in purchasing contracts, supplier questionnaires, external and internal audits. Suppliers are also required to have certain environmental certifications in order to be included in the bidding process. **Moreover, these measures apply to both direct (raw materials and energy) and indirect (professional services, packaging and transportation) suppliers.** DSM is also transparent on how environmental problems uncovered in the supply chain were addressed by corrective measures. In 2012, for example, one supplier did not pass the sustainability audit (received a D ranking), which meant that DSM had to freeze the contract with that supplier. For 13 suppliers, an improvement programme had to be agreed (B-C ranking).

## ● Top 20 Company performances on integrating social factors into supply chains

Title	Country	Sector	Sustainability Driver Score (/100)	Overall CSR Score (/100)	Market Cap (EUR bn)
Koninklijke DSM	Netherlands	Chemicals	92	63	9.666
Deutsche Telekom AG	Germany	Telecommunications	89	48	70.823
BT Group PLC	UK	Telecommunications	89	66	5.138
E.on SE	Germany	Electric & Gas Utilities	88	53	25.493
L'Oreal	France	Luxury Goods & Cosmetics	88	67	932
Kimberly–Clark Corp.	USA	Luxury Goods & Cosmetics	88	55	34.683
Geberit AG Reg.	Switzerland	Building Materials	87	59	12.101
Telecom Italia	Italy	Telecommunications	86	51	21.115
Air Products & Chemicals	USA	Chemicals	86	51	27.849
CRH plc	Ireland	Building Materials	85	59	21.056
Toto Ltd.	Japan	Building Materials	84	50	5.403
3M Co.	USA	Chemicals	84	52	89.942
Dell Inc.	USA	Technology–Hardware	83	48	n/a
Lafarge	France	Building Materials	82	63	17.512
KPN	Netherlands	Telecommunications	82	48	141
Symrise AG	Germany	Chemicals	81	60	7.340
Svenska Cellulosa B	Sweden	Forest Products & Paper	81	54	16.855
William Demant	Denmark	Health Care Equipment & Services	80	27	4.161
Henkel	Germany	Luxury Goods & Cosmetics	79	64	41.840
Red Electrica Corporación	Spain	Electric & Gas Utilities	79	68	9.909

### KEY FINDINGS

- **The top 20 companies all achieve advanced performances**, ranging from 79/100 to 92/100.
- The top 20 companies are **diverse in terms of their size, sector activities (8 difference sectors) and regional representation** (representation from North America, Asia Pacific and Europe).
- The **majority of the top 20 are European companies (75%)**.
- **Six companies appear in both, environmental and social, top 20 lists** (Koninklijke DSM, BT Group, Deutsche Telekom, Kimberly Clark, Telecom Italia and Symrise).
- **Some companies appear to actively and deliberately focus their CSR commitments and processes on this specific topic, with less reporting on other CSR issues.** For example, William Demant achieves an overall CSR score of 27/100, but is part of the top 20 companies on integrating social factors into supply chains (advanced score of 80/100). William Demant is a Denmark–based Company engaged in the development, manufacture and sale of equipment designed to aid people's hearing and communication. The company reports extensive measures on this topic including the contractual clauses with suppliers, dedicated supply chain audits and the provision of supplier support. The company states that it particularly focuses its attention on its Chinese suppliers. In 2014, it reported 14 CSR audits, nine of which were carried out by an external auditing firm. The nine external audits were followed up by internal audits, to control that initiatives contained in prior action plans had indeed been carried out.



## BEST PRACTICES ON INTEGRATING SOCIAL FACTORS INTO THE SUPPLY CHAIN

As seen for environmental factors, **Koninklijke DSM** demonstrates the most advanced performance (92/100).

- The company has issued a formalised and exhaustive commitment in its Supplier Code of Conduct. The Supplier Sustainability Program is steered by an internal working group and through a partnership with one NGO and one of its Suppliers, DSM has launched a programme to share insights and lessons learned with a group of suppliers. DSM reports comprehensive measures, including audits,

integration of social issues into contractual clauses, supplier questionnaires, and training of employees in charge of purchasing. DSM reports that these cover both direct (raw materials and energy) and indirect (professional services, packaging and transportation) suppliers and reports that all major social problems uncovered in the supply chain were addressed by corrective measures.

**ArcelorMittal** is an active participant in the OECD working group on implementing the due diligence guidelines for responsible mineral supply chains.

- This group aims to define an approach to the management of tin supply chains for minerals in the Great Lakes region of Africa. The company also supports the Conflict Minerals Due Diligence Process as outlined in the OECD guidance, and has requested its suppliers to apply the principles set out in ArcelorMittal's code for responsible sourcing. It has engaged with customers, suppliers, peer companies, and NGO experts in drawing up this code.

- The company also states it continues to participate in the UN Global Compact Supply Chain working group, and co-leads the CSR Europe working group on sustainable supply chains, and business and human rights. Moreover, a new Centre of Excellence was created in the company's purchasing organisation at the end of 2012. One of its objectives is the consistent and systematic monitoring of responsible sourcing performance of the company's global suppliers.

**Philip Morris International (PMI)** reports exhaustive awareness-raising, selection and collaboration measures to address labour standards in its supply chain. This includes:

- Creation of Farm Profiles, done through site visits using a tool developed together with the labour rights NGO Verité (gathering information about the type of labour employed, farming activities that minors may be involved in, and hiring practices). Based on the Farm Profiles, PMI and suppliers identify risks and improve its programmes;
- Training programmes for leaf buying teams and suppliers on the Code's principles and standards and the various issues related to agricultural labour practices;
- Country teams conduct unannounced visits to farms to assess 'prompt action issues' (i.e. situations where workers' well-being is at risk, vulnerable groups are in danger, forced labour);>
- Compulsory implementation of the Agricultural Labour Practices Code for all farmers who have contractual arrangements directly with PMI or with third-party leaf suppliers who buy tobacco for PMI;

- Changing its leaf buying model to more direct buying in Malawi, the Philippines and Indonesia, leading to the implementation of the programme at more farms in those countries;
- Grievance mechanisms such as in Kazakhstan, PMI worked with Local Communities Foundation (LCF),

an NGO that monitors the treatment of Kyrgyz migrant workers on Kazakhstan’s tobacco farms, provides advice and support and a grievance mechanism. LCF conducts regular farm visits with a team of qualified professionals and manages a hotline to report problems.

**Kimberly Clark** states that all major social problems uncovered in its supply chain were addressed by corrective measures. The company reports that as part of its auditing there has been one internal or

third-party audit finding to date that highlighted freedom of association and collective bargaining issues. All findings are reported to have been fully remediated.

## ● Level of exposure to environmental and social controversies in supply chains

### KEY FINDINGS

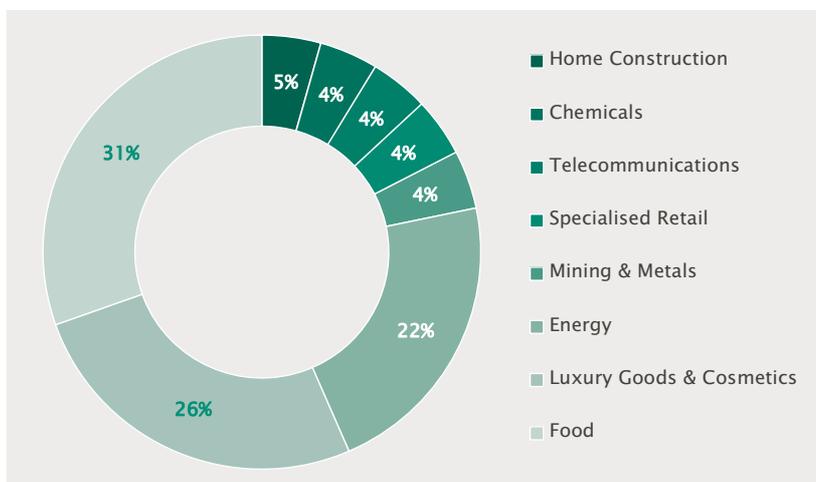
- Controversies such as the Rana Plaza collapse in Bangladesh, the slavery concerns in the Thai prawn supply chain and environmental impacts of palm oil production are receiving wide media coverage. However, **relatively few companies actually face direct supply chain allegations**:
  - When compared to the 38 different sustainability drivers assessed by Vigeo (covering the full spectrum of CSR topics including Human Resources, Business Behaviour, Corporate Governance, Human Rights, Community Involvement, Environment), direct allegations linked to companies' responsible supply chain management are amongst the least frequently identified.
  - On a global scale, **6.9% of the companies face allegations concerning breaches of social standards in the supply chain**. This number decreases to 2.2% when it concerns allegations linked to environmental standards.
- It is still **rare that companies face legal cases related to environmental and social standards in their supply chains**, however there are an increasing number of examples (see next pages for examples).
- This indicates that supply chain management remains a marginal topic in the CSR and consumer arena.
- The Specialised Retail is the sector most exposed to social supply chain allegations** (24% of all allegations). Along with Supermarkets, Food and Beverage, they account all together for 57% of social supply chain allegations identified.
- Food is the sector most exposed to environmental supply chain allegations** (31% of all controversies). Along with Luxury Goods & Cosmetics and Energy they all account for 79% of all environmental supply chain allegations identified by Vigeo Eiris.

## EXAMPLES OF SECTOR-WIDE ENVIRONMENTAL SUPPLY CHAIN CONTROVERSIES AND COMPANIES' RESPONSES

### SOURCING OF PALM OIL

- The Food and Luxury Goods & Cosmetics sectors** continue to face high profile and recurrent allegations linked to the sourcing of palm oil. In particular, as the Round Table on Sustainable Palm Oil (RSPO) celebrates more than 10 years (launched in 2004), questions over the efficacy and integrity of the initiative continue to be raised by various stakeholders<sup>(11)</sup>.

### ● ENVIRONMENTAL CONTROVERSIES IN SUPPLY CHAIN



<sup>(12)</sup> In this context it is interesting to note that in January 2015, the Malaysian Government launched its own palm oil standard called the Malaysian Sustainable Palm Oil (MSPO). Whilst this standard is broadly in line with the RSPO, there are some differences. For example, whilst the RSPO is extremely restrictive on cultivation around peat lands, the MSPO standard remains more in line with Malaysian national regulation that allows for cultivation dependent on the depth of the peat land. This move from the Malaysian state has been supported by multinationals as it gives further legislative 'teeth' to the RPSO standard in Malaysia, however there is concern that the two standards are not directly aligned with the MSPO being considered as weaker.

<sup>(13)</sup> For example, 'TFT suspend PT SMART membership' – TFT – 19/05/2015; 'Response to The Forest Trust statement on 19 May 2015' – GAR – 20/05/2015

- Companies continue to face allegations concerning deforestation, forced resettlements of communities, slash and burn techniques, abuses by security forces and harvesting palm oil in protected national forests. A number of companies (including Golden Agri Resources, Cargill, Kellogg, L'Oreal, Procter and Gamble, Hershey, Wilmar International, Unilever, Danone, Nestlé) responded with revitalised and more ambitious commitments in order to mitigate widespread concerns and breathe new life into

the RSPO initiative. The revised commitments are predominantly linked to improving the traceability of supply chains within a much shorter time frame than many companies had originally planned and have often been developed with relevant stakeholder organisations, such as the 'The Forest Trust' (TFT). These revised policies and initiatives are indicators of a positive shift. However, despite these steps, the continuing allegations indicate that the sustainability of this industry remains a long term challenge.

## ANIMAL WELFARE

- The **Luxury Goods & Cosmetics** sector continues to face controversies linked to animal welfare with mixed reaction from the companies' involved. For example, three animal rights organisations (L214, Last Chance for Animals and Animal Equality) launched a website in September 2014 and a petition to make several companies stop selling fur (including Louis Vuitton, Dior and Marc Jacobs, owned by LVMH, Burberry and Yves Saint Laurent, owned by Kering). The three organisations conducted a two year undercover investigation into the conditions at 70 rabbit breeding farms in Catalonia, Spain, and published a video about the allegedly cruel conditions at these farms. Animal Equality claims they tried to engage with the companies to make them discontinue all sale of

fur before the publication of their investigation results, but was not satisfied with the companies' responses and thus decided to launch the campaign to inform the public to try to influence consumer decisions. In response to these allegations all companies denied they sourced rabbit fur from the farms accused of animal cruelty<sup>(14)</sup>. Another campaign was led by PETA who urged major retailers to ban rabbit fur because of its cruel farming practices in China (which supplies 90 percent of the world's angora). Following this campaign a number of brands have banned the use or sale of angora wool (including Inditex, Forever 21, Lands' End, Calvin Klein, Tommy Hilfiger and Lacoste).<sup>(15)</sup>

## ENVIRONMENTAL POLLUTION

- In the **Energy sector**, companies are often affected by subcontracting companies facing recurrent convictions for causing environmental spills and pollution. Energy companies (upstream and downstream) rely heavily on suppliers and contractors for various products and services, such as exploration services, engineering, construction

and equipment, as well as drilling & production support. Examples of companies linked to such controversies are Chevron, BP, Talisman Energy, Marathon Oil. Usually such cases are subject to legal proceedings where claims are filed against both subcontractors and the 'sourcing' companies. A majority of these cases have received settlement agreements and compensatory claims are being paid while both companies and subcontractors

<sup>(14)</sup> "Fourrure : des images insoutenables impliquant Armani, Yves Saint Laurent, Christian Dior, Louis Vuitton" – L214 – 03/09/2014 ; "Rabbits Tortured on Fur Farms for Major Fashion Designers" – Animal Equality – 12/09/2014; "Saint Laurent, Burberry And Dior Deny Animal Cruelty" – Vogue – 16/09/2014

<sup>(15)</sup> 'Zara Urged To Drop Orders For Angora Rabbit Fur Following Claims Of Animal Torture' – Business Insider – 16/12/2013; 'Can angora production ever be ethical?' – The Guardian – 16/12/2013; 'Zara and Gap finally ban angora as shoppers threaten to boycott shops over the horrific plight of rabbits plucked alive for their fur' – Daily Mail – 27/12/2013

<sup>(16)</sup> "BP settlement will cost \$20.8 billion, Justice Department says" – Washington Post – 05/10/2015; "U.S., BP Finalize \$20.8 Billion Deepwater Oil Spill Settlement" – Wall Street Journal – 05/10/2015

tors are ordered to adopt court-enforceable measures to improve operational safety and emergency response capabilities. For example in BP's civil lawsuit following the Macondo oil spill in 2010 it was concluded finding that BP acted with gross negligence and wilful misconduct in its actions leading to the disaster. Alongside the finding of BP's own direct responsibility, the Judge also ruled that the division of responsibility between BP and its contractors stood at 67% BP, 30% Transocean, and 3% Halliburton. In October 2015,

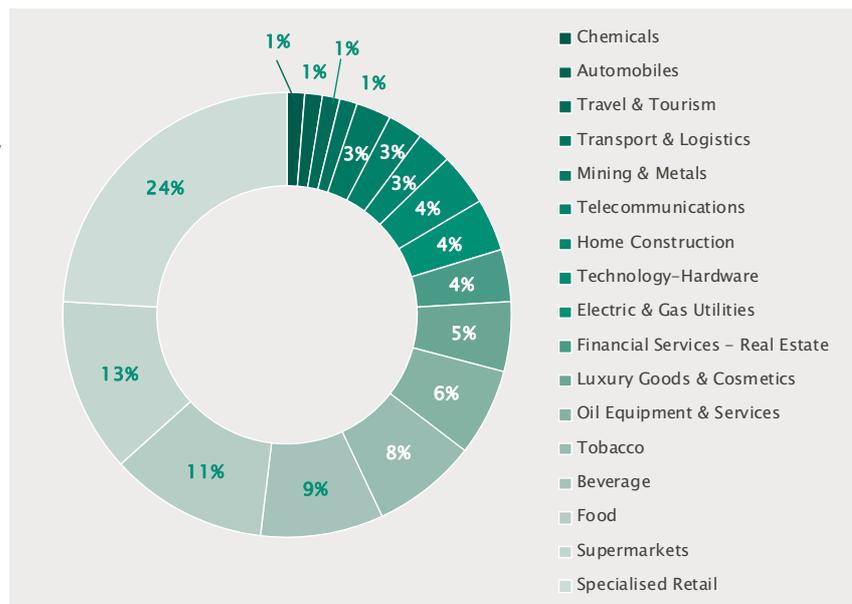
BP reached a final settlement of USD 20.8 billion for the violation of the Clean Water Act and to settle claims from the United States, Gulf Coast states and local entities. The Clean Water Act fine is the largest in history. BP's own investigation highlighted the strengthening contractor management as one area needing action<sup>(16)</sup>. This major event demonstrates that the energy sector has vast and costly impacts not only through its own operations but also through its subcontractors' activities, thus placing the sector as the third

## EXAMPLES OF SECTOR-WIDE SOCIAL SUPPLY CHAIN CONTROVERSIES AND COMPANIES' RESPONSES

### RANA PLAZA COLLAPSE

- In the most exposed sector, Specialised retail, many companies continue to face controversies linked to the safety of the factory buildings where textile suppliers are housed. For example, this sector was at the heart of the Rana Plaza disaster in Bangladesh in April 2013. The building housed five garment factories and more than 2,500 people were estimated to be working to manufacture clothing for apparel and retail companies. This event triggered a widespread concern about the safety of those working in textile factories in Bangladesh<sup>(16)</sup>. Following this, in 2014, over 170 international brands and retailers signed the final Bangladesh Accord on Fire and Building Safety. Under the Accord trade unions and multinational companies are proactively working together to improve the precarious situation of more than 2 million garment workers in Bangladesh. Alongside this agreement, some

### SOCIAL CONTROVERSIES IN SUPPLY CHAIN



companies are facing ongoing lawsuits based on accusations that they breached their duty to workers in the building by failing to implement standards and oversight mechanisms designed to ensure the health and safety of workers who manufactured clothing for their stores<sup>(17)</sup>.

<sup>(17)</sup> For more details on the role of trade unions, NGOs and the ILO in this Accord, please refer to Chapter 2, section on "Role of stakeholders in maturing companies' supply chain practices".

<sup>(18)</sup> Wal-Mart, J.C. Penney and Children's Place sued by victims of 2013 Bangladesh factory collapse"- Dallas News-27/04/2015 - "J.C. Penney says it didn't have suppliers in collapsed Bangladesh factory"- Dallas News- 29/04/2015

## 'SLAVERY' SCHEMES IN INDIA TEXTILE INDUSTRY

Concerns in the Specialised Retail sector's supply chain are certainly not limited to Bangladesh or only to health and safety conditions. There are also allegations of ongoing forced and bonded labour, for instance in textile mills located in Tamil Nadu, India, a hub in the global textile and knitwear industry. There are reports that some mills use the so-called 'Sumangali Scheme', a practice whereby young women and girls from poor families are promised decent jobs away from home and a lump sum when their contract is complete, but instead are forced to work without a contract or pay slips up to 60 hours a week or more all-year-round. Primark (part of Associated British Foods) was identified as the major buyer of one of the investigated mills (Jeyavishnu) and as a client on another mill (Sulochana). The Company denied any links to the Sulochana mill, but acknowl-

edged that contractors supplying apparel source from Jeyavishnu and cited its 'Fair Hiring, Fair Labour' programme (launched in 2012, together with US-based NGO Verité) was in place to build management systems capacity and internal self-monitoring, provide practical guidance for recruiters, screen brokers and labour agents, and provide on-site management and monitor hostel management. Primark further said that it had implemented a project at the Jeyavishnu facility in 2013, with a focus on compliance with working hours, the provision and use of personal protective equipment, employment contracts, health and safety training, and clean hostel facilities. Primark did also report to the author of the report that "there remain some serious concerns in relation to working practices at this site" (*"Flawed Fabric - SOMO and India Committee of the Netherlands" - October 2014*).

## THAI PRAWN 'SLAVERY'

- The second most exposed sector is Supermarkets and an ongoing controversy impacting this industry is linked to the Thai Prawn supply chain. This is one example that demonstrates the exposure that this sector faces, where supply chains are not only hugely varied (due to the vast range of products sold by supermarkets), but are also hugely complex, thus posing risks at various operational and geographical stages. An investigative report published by The Guardian alleged that slavery, human trafficking and forced labour is used by suppliers are involved in the production of prawns for supermarkets including Wal-Mart's Carrefour, Costco, Tesco, Morrison, Seven Eleven, Woolworths and Colruyt. After tracing supermarkets' food<sup>(19)</sup> chain from boat to shelves, The Guardian reported to have uncovered a Thailand-based supplier, Charoen Pokphand (CP) Foods, sourcing fishmeal to feed its farmed prawns from suppliers that own, operate or buy

from fishing boats manned with slaves. The investigation recounts incidents of human trafficking in which men from Cambodia and Burma were hired on fishing vessels but were later found to be held against their will, bought and sold as slaves for extended periods at sea and without pay. This is in addition to reports of 20-hour shifts, regular beatings and torture, executions and work under mental and physical threat. CP did admit to the Guardian, that slave labour is part of its supply chain and that CP then supplied international supermarkets with frozen or cooked prawns. All affected companies responded that they condemned slavery and human trafficking for labour and conducted rigorous social audits. However, the report identified that retailers efforts up until this report appeared to more focused on abuses that came to light further up the Thai prawn supply chain - in processing and packing factories or in companies subcontracted to peel prawns.

<sup>(19)</sup> 'Revealed: Asian slave labour producing prawns for supermarkets in US, UK' - The Guardian - 10/06/2014

<sup>(20)</sup> For more details on this case, please refer to Chapter 1 on the 'How does the location of headquarters influence companies' behaviour?'

<sup>(21)</sup> In October 2011, SOMO alleged that on tea plantations in India and Kenya, which supply tea to Unilever, working conditions were found to be 'problematic' due to issues related to wages, discrimination, casual workers and the application of pesticides without protective gear. In August 2013, a TV broadcast by ARTE reported that sexual harassment continued to be an issue at Kericho. In response to the allegation, Unilever reported to have independently audited the plantations and integrated a range of corrective measures, including improved grievance processes, tailored training, a new compliance officer, significant changes in the Team Leaders' gender balance and scope of responsibility.

<sup>(22)</sup> In January 2012, the International Labour Rights Forum threatened Hershey to air a commercial titled "Hershey's Chocolate: Kissed by Child Labour" at the Super Bowl. Following the International Labour Rights Forum campaign threat, Hershey disclosed a commitment to source only independently certified cocoa (by the Rainforest Alliance) for its line of Bliss chocolates. In response to this announcement, the International Labour Rights forum did not publically air the documentary.

## LABOUR STANDARDS IN COMMODITIES SUPPLY CHAIN

- Likewise in the Food sector, emblematic products such as coffee, chocolate and sugar cane are sourced from countries where fundamental human rights and labour standards are not always respected, promoted or fully enforced. Production of such commodities is often run by small-scale farms where temporary or seasonal work, weak remuneration, subcontracting, immigrant workers and child labour have been reported. Furthermore, farms are spread over wide geographical areas, where trade union and cooperative organisation is less common. For those reasons, the integration of social factors in supply management is one of the key issues for food companies.
- Allegations of using child labour are particularly common in the cocoa supply chain and have frequently been linked to companies operating in this industry (for example the ongoing lawsuit filed under the Alien Tort Claims Act against Nestlé USA, Archer Daniels Midland and Cargill<sup>(20)</sup>, ongoing concerns in Unilever’s tea leaf supply chain<sup>(21)</sup> and recurrent criticism against Hershey<sup>(22)</sup>). A number of companies are reporting steps to identify and respond to these challenges. For example, Nestlé asked the Fair Labor Association to conduct an independent investigation into its cocoa supply chain from its headquarters to the farms in Ivory Coast, which led to the identification of numerous violations of its labour code, especially with regard to child labour. Nestlé is fully transparent on these findings and reports on corrective measures.

## BEER GIRLS IN CAMBODIA

- In the Beverage sector, which is the fourth most exposed sector to social allegations, the ‘supply’ chain challenges are not only upstream (where they share similar challenges as food and supermarkets companies) but also downstream as a major challenge in some countries is the protection of individuals who are actually selling final products. For example, since 2010 several NGO reports have demanded that international breweries more actively tackle the problem of Cambodian girls selling their beer, which are still reported to be putting up with violence, sexual harassment, forced drinking, and even rape on the job. In response to these concerns an industry initiative was established in 2006, The Beer selling Industry Cambodia (BSIC), in order to improve the health, safety and working conditions through the application of a Code of Conduct and a range of awareness campaigns. According to an independent assessment in 2014, the working conditions of beer promoters who belong to the BSIC have improved significantly over the past three years, with improvements reportedly made in the beer promotion work, including awareness of workers’ rights, lower alcohol consumption, less instances of prostitution and less cases of sexual harassment (*BISC website – accessed 02/06/2015 – <http://www.bsic.com>*).

## TOWARDS MORE EFFECTIVE MANAGEMENT OF SUPPLY CHAINS?

This chapter focusses on three specific areas of action that companies' can move towards to ensure more effective management of environmental and social factors in their supply chains:

- Enhancing audit mechanisms (ensuring exhaustive scope, coverage and systematic implementation of corrective measures when problems are revealed);
- Building active relations with key stakeholders, such as unions;
- Building enduring, balanced and fair relations with all suppliers.

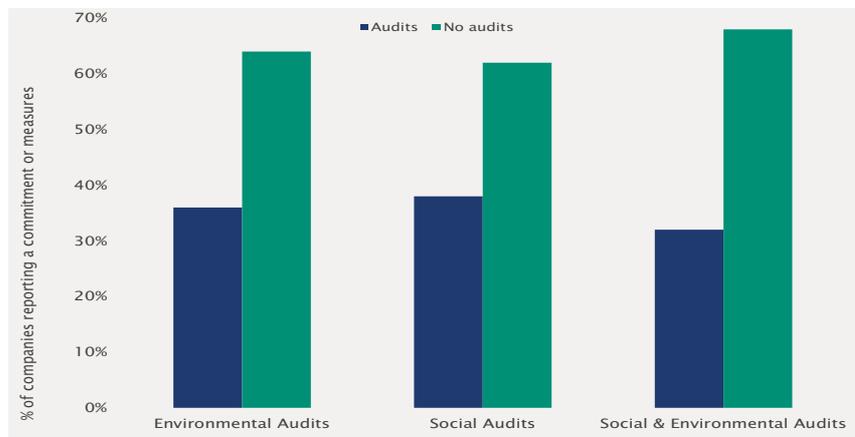
These are identified as actions that are currently scarcely reported, but that are increasingly recognised as strategic for companies to move beyond short term, reactive, reputation-building models to a more robust approach that can better mitigate risks and seize opportunities both for vulnerable stakeholders and for the companies themselves.

### Deployment of Audits

#### KEY FINDINGS

- **More than a third of companies do report to have implemented audits.** Audits are not the only possible approach, but are considered an important part of supply chain risk management as they offer a snapshot into a supplier's business in order to identify any non-compliances with companies' codes and values, and areas that are in need for improvement.
- However, **there is a lack of assurance on the topics covered by these audits, on the independence of auditors and on the systematic follow up if incidents are identified** (see next pages for details).
- There is a relatively **homogeneous approach towards both social and environmental audits:** 37% of the companies report to audit their suppliers on environmental standards, while 38% report on social audits. 32% of the companies report audits on both environmental and social standards in the supply chain.
- There are **very heterogeneous performances across sectors.** Tobacco and Specialised Retail have the largest percentage of companies reporting environmental audits (62% and 60%), while

#### PERCENTAGE OF COMPANIES REPORTING SOCIAL AND ENVIRONMENTAL AUDITS



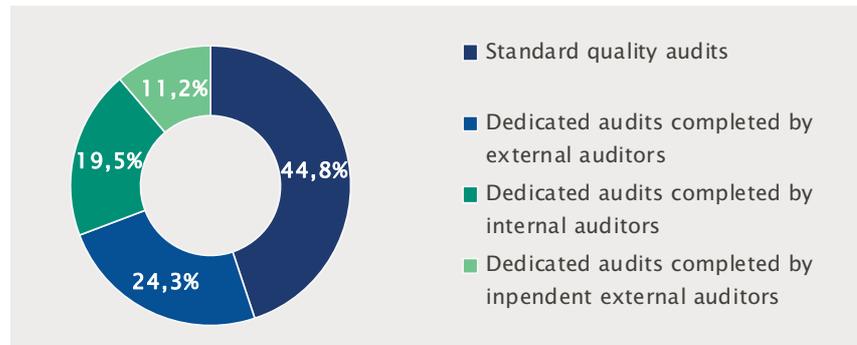
Business Support Services are placed as the laggards (7%). Regarding social audits, Technology-Hardware and Beverage are the leading sectors, with, respectively 77% and 70% of companies reporting on such measures, while Home Construction and Business Support Services appear as the weakest sectors (13% and 14%). This heterogeneity across sectors can be explained by differences in exposure regarding environmental and social risks in the supply chain, where higher exposure appears to lead to more implementation of audits, at least when considering the leaders and laggards.

## ● Scope and Independence of Audits

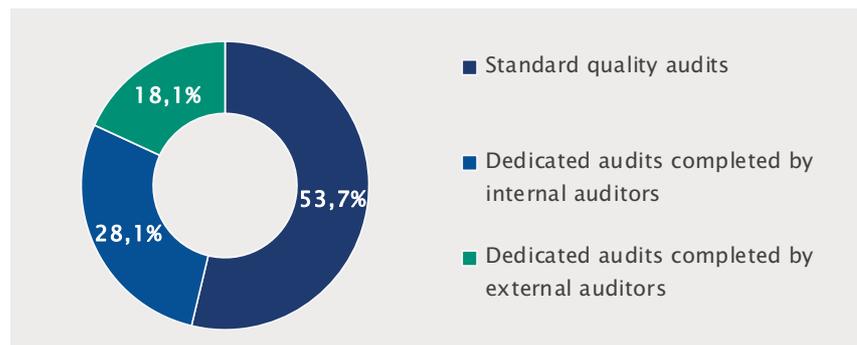
### KEY FINDINGS

- A minority of companies provide evidence that they use external auditors (18% for environmental, 35.5% for social).
- The sector with the highest percentage of companies declaring to have independent external social audits is Specialised Retail (18.5% of companies). An independent auditor is an organisation that is not hired by the company, such as a specialised NGO (for example, Fair Labour Association, Fear Wear Foundation).
- However, only a minority of these specialised retail companies report on what social topics are actually covered by these audits. This is a concern because implementing irrelevant audits might mean that audits fail to check crucial topics (such as building safety in the Rana Plaza collapse).
- Of those companies who do specify what topic are covered, the most recurrent social issues reported to be checked are child labour, forced labour and health and safety. Fundamental labour rights, such as freedom of association, collective bargaining and non-discrimination appear to remain out of scope. This is cause for concern because having free, independent and active employee representative organisations and bodies within a supply chain site is a critical tool to ensuring supply chain viability. It also ensures

### ●● SOCIAL AUDITS



### ●● ENVIRONMENTAL AUDITS



reliable, objective reporting and follow-up of concerns.

- The two sectors with the highest percentage of companies declaring to have external environmental audits are Tobacco and Specialised Retail. However, as for the social audits, the majority of these companies do not appear to specify the environmental standards included in their dedicated environmental audits, which means there is a low level of assurance that relevant environmental topics are covered by these audits.

## ● Follow-up of incidents

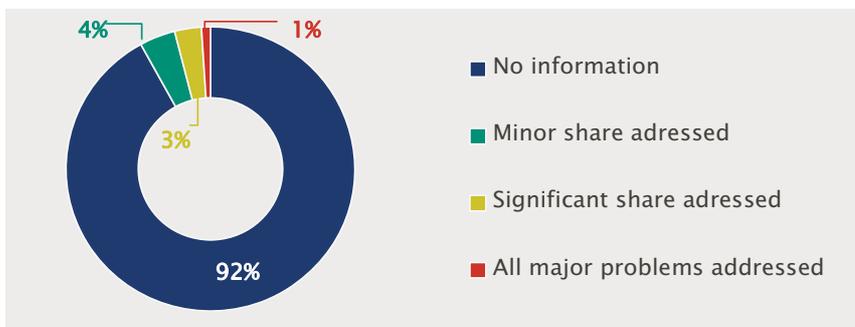
### KEY FINDINGS

- **The vast majority of companies do not report that they have implemented corrective measures for any social or environmental incidents identified in their supply chains.** This is a concern because a lack of follow up can completely undermine the utility of audits and any other measures installed.
- **This weak overall reported approach is similar for environmental and social challenges:** 11% of companies disclose evidence that they have applied corrective measures for at least a share of social incidents identified, with 8% of companies for environmental incidents.
- **Building Materials and Technology–Hardware** are the two sectors with the highest percentage of companies reporting to have corrective measures to address social incidents in their supply chains (37.5% and 17.9% respectively).

### ●● PERCENTAGE OF COMPANIES REPORTING CORRECTIVE MEASURES TO SOCIAL PROBLEMS IDENTIFIED



### ●● PERCENTAGE OF COMPANIES REPORTING CORRECTIVE MEASURES TO ENVIRONMENTAL PROBLEMS IDENTIFIED



- The sector with the highest percentage of companies reporting to have corrective measures to address environmental incidents in their supply chains is **Luxury Goods and Cosmetics** (17.2%).

### EXAMPLE OF BEST PRACTICES

- **Geberit AG Reg.** according to the company, shortcomings were revealed at three Chinese suppliers in 2013, primarily in the areas of occupational safety, working hours and remuneration. Action plans were agreed upon with these three suppliers, the implementation was checked during a re-audit in 2014.
- **Lafarge** stated that a scorecard is provided with each assessment performed. The assessment is reviewed with suppliers and corrective actions are then implemented. Typically, a score below 24 requires a corrective action and requires the

Country and Central Teams to work with suppliers accordingly. In 2014, the company reported that it had 1 corrective action plan formally submitted.

- **LVMH** reports that 40% of its 750 supplier audits identified minor non-compliance issues, 3% identified major non-compliance issues, 19% indicated a need for significant improvement by suppliers. In all, 208 corrective action plans were implemented at its suppliers.
- **Kimberly-Clark** reported that 100% of suppliers successfully remediated violations in 2012, 13% of whom faced follow up audits.

## ● Role of stakeholders in maturing companies' supply chain practices

### KEY FINDINGS

- Although there are some best practices (such as Inditex), **overall there is a lack of evidence that companies are engaging with stakeholders** (such as NGOs and trade unions) to better manage their supply chains in order to avoid environmental and social dumping, as well as to enhance global standards across value chains.
- **There appears to be a slightly more proactive approach to partnerships between European companies and stakeholders, compared to companies from other regions.** Of those reporting to develop policies with stakeholders, 2.7% are companies based in Europe while 1% are listed in North America and only 0.09% (1 company) is listed in the Asia Pacific region.

### BEST PRACTICE

#### GLOBAL FRAMEWORK AGREEMENT BETWEEN INDITEX AND INDUSTRIALL GLOBAL UNION

*“ The ground-breaking agreement between IndustriALL Global Union and Inditex, which was renewed in 2014, is the first of its kind to cover a retail supply chain.*

*It underlines that freedom of association and the right to bargain collectively play a central role in a sustainable supply chain because they provide workers with the mechanisms to monitor and enforce their rights at work.*

*Under the GFA, which was originally signed with IndustriALL's predecessor the International Textile, Garment and Leather Workers' Federation in 2007, Inditex recognizes IndustriALL as its global trade union counterpart. Both parties undertake to collaborate to ensure the sustainable and long-term observance of all international labour standards across Inditex's operations, including its suppliers.*

*Inditex's Code of Conduct for External Manufacturers and Suppliers underpins the agreement which outlaws forced labour, child labour, discrimination and harsh and inhumane treatment throughout the Inditex supply chain. It provides for the payment of a living wage for a standard workweek, limitations on working hours, healthy and safe workplaces, regular employment*

*and environmental awareness. The terms of the agreement apply equally to direct suppliers, contractors and sub-contractors including homeworkers. No subcontracting is allowed without the prior written consent of Inditex and suppliers allowed to subcontract will be responsible for subcontractor compliance.*

*Recognizing the role of organized labour and collective bargaining, Inditex and IndustriALL will keep constantly under review developments in this area in the Inditex supply chain and will co-operate in finding solutions where problems are detected, including collaborating on training programmes for management and workers.*

*To facilitate this ongoing review Inditex will provide IndustriALL with relevant information on its supply chain and both Inditex and IndustriALL will jointly develop training policies and programmes to drive compliance.*

*The application of the agreement will be reviewed annually by a six person group drawn jointly from Inditex and IndustriALL”*

Global Framework Agreement Inditex – consulted September 2015 – <http://www.industrial-union.org>

## KEY STAKEHOLDERS IN MATURING COMPANIES' SUPPLY CHAIN PRACTICES

**Non-governmental organisations (NGOs)** have played a major role in pushing for sustainable development at the international level. Campaigning groups have often been key drivers of inter-governmental negotiations, ranging from the regulation of hazardous waste to a global ban on land mines and the commitment to eliminate slavery<sup>(23)</sup>. Even those businesses that do not specialize in highly visible branded goods are feeling the pressure, as campaigners develop techniques to target downstream customers and shareholders. In this context, the new wave of business-NGO collaborations differs from the relationships of the past. No longer is corporate philanthropy the main driver for collaboration. We are now seeing the birth of strategic partnerships that are designed to tackle both internal operational issues and the external impacts of corporate activity, including the impacts in the supply chain.

- Examples include the Fairtrade Foundation, Ethical Trading Initiative (ETI) and the World Wide Fund for Nature (for example, creating the Forest Stewardship Council accreditation, certification and labelling scheme). However, alongside these developments and on a more critical note, collaboration between businesses and NGOs can be controversial, and pose significant challenges to the participants, as they can compromise the autonomy of NGOs and even the credibility of labels. One such initiative that has received this type of criticism was developed by the US-based Rainforest Alliance and the US-based corporation Chiquita Brands International, who created a certification scheme for banana plantations called 'Better Banana' project (BBP). The Rainforest Alliance is an organisation dedicated to 'the conservation of tropical forests

for the benefit of the global community'. Meanwhile Chiquita, one of the largest agricultural firms in the world, was Costa Rica's third largest banana exporter in 1999, accounting for more than 18% of the total USD 623 million worth of exports. Some critics believed that the Rainforest Alliance became financially dependent on Chiquita, and was thus allegedly beholden to follow the company's directions. Although incidents of non-compliance with the standard (such as aerial spraying while workers were in the fields) were reported, no 'de-certifications' were made, affecting the NGO's role as a credible auditor in this situation.

- **Trade unions** can play a positive role in building more sustainable business practices. Having free, independent and active employee representative organisations and bodies within a supply chain site is a critical tool to ensuring supply chain viability. It also ensures reliable and objective reporting and follow-up of concerns. For example, the tragic factory fires in Pakistan and Bangladesh in 2012, and the Rana Plaza factory collapse in 2013, were the tipping point that brought together various stakeholders to improve labour practices in the textiles and clothing industries. Unions in particular play an important role in the Bangladesh Accord on Fire and Building Safety. The final Accord is a legally binding agreement between international trade unions IndustriALL and UNI Global, Bangladesh trade unions, and international brands and retailers. International NGOs, including the Clean Clothes Campaign and the Workers' Rights Consortium, International Labour Rights Forum and Maquila Solidarity Network are witnesses to the agreement. Unions alleged that the industry relied on one-off safety audits in its factories,

<sup>(23)</sup> « Opposites attract », Jem Bendell, *IISD's Business and Sustainable Development*, 2013

<sup>(24)</sup> Company representatives include PVH, H&M, Inditex, Tchibo, C&A, Ootto Group - Trade union representatives include Uni Global Union, IndustriALL global union, United Federation of Garments Workers, nat.Garment Workers Fed.

conducted by auditing companies that are created and funded by the brand themselves. As partners in the Accord, the trade unions are therefore in a position to contribute to better accountability and monitoring of conditions. The Accord is governed by a Steering Committee with equal representation of the signatory companies and trade unions with a neutral Chair provided by the

International Labour Organisation (ILO)<sup>(24)</sup>. Up to 2015, a total of 1498 factories have been inspected, representing about one third of the Bangladeshi textile industry. After an inspection, factories and brands are tasked to submit a Corrective Action Plan for approval to the Accord.

## ● Promotion of sustainable relations with suppliers

### OPPORTUNITIES FOR COMPANIES

The maintenance of balanced and fair relations with suppliers is considered as a way for companies in highly exposed sectors to ensure enhanced risk management of their supply chains. These relations with suppliers can help to avoid disruption by ensuring sufficient quality supply (by paying suppliers on time they can maintain economic viability and thus ensure continual operations). Such relations can also allow companies' to have better knowledge of the social and environmental risks

and even to help their suppliers to progress towards the implementation of more sustainable approaches. This is one of the conclusions displayed in the guidelines developed after the ILO-OECD Roundtable on Responsible Supply Chains in the Textile and Garment Sector, which stated that the reinforcement of relationships with suppliers can help companies to have a cohesion of policies and due diligence practices across their business partners.

## WHY FOCUS ON AGRICULTURAL AND TEXTILE SECTORS?

- **Huge and global spread of these supply chains** resulting in vast environmental and social challenges<sup>(25)</sup>;
- **High supplier vulnerability:** suppliers are confronted with major economic challenges in their everyday business (such as producing the range and quantity requested within tight delivery times, facing severe competition, receiving late payments, cancellation of orders and having to bear the costs of waste and forecasting errors); As lower costs mean better profits for companies, there is a risk of predatory behaviour and unbalanced demands on suppliers to meet the companies standards;
- Many international initiatives: for instance, the OECD and the ILO organized a roundtable in 2014 on responsible supply chains for the textile and clothing sector; the FAO–OECD Guidance for

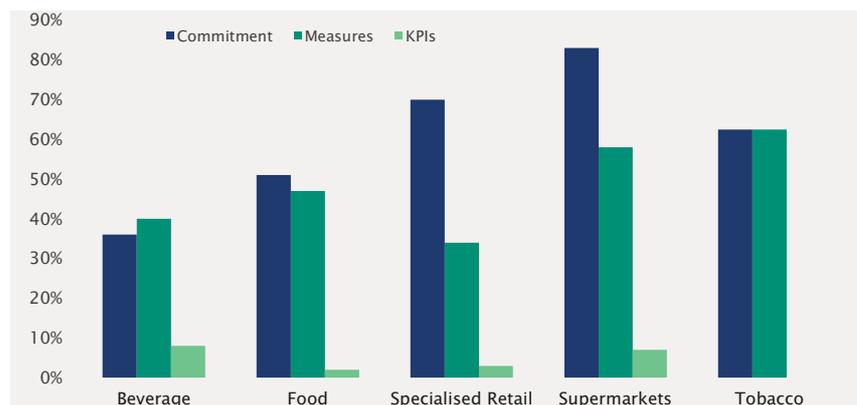
Responsible Agricultural Supply Chains<sup>(27)</sup>; the first UN Global Compact sector specific guidelines focussed on Food and Beverage sectors published in 2014<sup>(28)</sup>;

- Investor attention: for instance of the ten current Collaborative engagements coordinated by the UN PRI, three are linked to agricultural topics: Engagement with food, beverage and textiles sectors on improving the management of water risks within companies' agricultural supply chains; working group which is pushing for improvements in company practices across the value chain, in order to support the development of a more sustainable palm oil industry; engagement with food and beverage companies on working conditions in agricultural supply chains.<sup>(29)</sup>

## KEY FINDINGS

- Overall companies still achieve weak average performances towards ensuring sustainable relations with suppliers. Indeed, approximately 30% of companies in these sectors do not report on any commitments and measures to address this topic.
- Companies appear to focus more on selecting and controlling suppliers on social and environmental standards, than on developing fair and balanced relations with suppliers.

### PERCENTAGE OF COMPANIES REPORTING POLICIES, MEASURES AND KEY PERFORMANCE INDICATORS ON SUSTAINABLE RELATIONS WITH SUPPLIERS



<sup>(25)</sup> Currently almost 40% of ice free land is used for agriculture, this is the largest human endeavor on the planet. The population forecast for 2050 is 1 billion, 35% increase compared to today and in order to meet this population increase the earth will need to produce double the amount of crops.

<sup>(26)</sup> Please refer to Chapter 1 section called 'Level of exposure to environmental and social controversies in supply chains' for more information.

<sup>(27)</sup> FAO–OECD Guidance for Responsible Agricultural Supply Chains –www.fao.org – accessed 04/09/2015

<sup>(28)</sup> Food and Agriculture Business Principles – UN Global Compact – 2014

<sup>(29)</sup> UNPRI website – http://www.unpri.org – accessed February 2016

## KEY FINDINGS

- **Overall, companies report more systematically on their policies rather than on the measures that have been implemented to ensure fair and balanced relations with suppliers** (examples of measures: complaints management system for suppliers, risk maps for financial dependency, training for the purchasing department of sustainable relations with suppliers).
- **There is also a lack of disclosure on key performance indicators** (indicators such as the average payment delays, the total of suppliers income). No sector has more than 8% of companies reporting these KPIs.
- **Only 5.5% of companies in these sectors face allegations regarding their relations with suppliers.** However media attention on sustainable relationships with suppliers is increasing. There is now large social debate and sector side concern (for example, on milk prices in the UK) and there are now a number of allegations emerging (for example, Tesco and Diageo – see below for details).
- Although still weak in absolute terms, **the Supermarkets sector achieves the best performance on developing sustainable relations with suppliers.** Thanks to their size and market dominance, companies in this sector can hold significant power over suppliers. For instance, Consumers International (CI), the world federation of consumer groups, have raised concerns about the growing market concentration of the supermarket sector in Europe, as the largest five supermarket chains account for over two thirds of the grocery market, which increases the power of big players over smaller suppliers. In this regard, the British Government established a supermarket ombudsman, the Groceries Code Adjudicator, to monitor the respect of its code of practice that govern the relations between the major supermarkets and their suppliers. Other European countries have now implemented initiatives to address the issue, such as Spain, France and Germany<sup>(30)</sup>.
- After Supermarkets, **Specialised Retail is the sector with the second highest percentage of companies reporting a commitment to ensure sustainable relations with suppliers.** Due to the vast and diversified supply chains of these retail companies, suppliers in this sector usually face high competition and intense demands. There are some sector wide initiatives to respond to these challenges. For instance, the 126 signatories of the European DIY Retail Association's Pan-European Code of Practice on Retailer/Supplier Relations have committed to issues such as the respect of contractual obligations and payment delays. However, the sector appears to be better at articulating policies than at concretely implementing measures, as only 34% of companies reports on related measures.
- **Tobacco is the sector with the highest number of companies reporting measures to address this topic.** Tobacco companies are dependent on one main ingredient for their business, the tobacco leaf. This means that if leaf farmers' are unable to meet their demands, companies' own production would be severely compromised. This is also a sector that is highly scrutinised due to the impact of its products on human health, thus by reporting on its approach to supply chain management these companies' may be seizing opportunities to counter their negative reputation.
- **Food and Beverage are the sectors where this issue appears to be the worst addressed.** Half or less of the companies in these sectors report any policy or measures to ensure sustainable relations with suppliers.

<sup>(30)</sup> *'The relationship between supermarkets and suppliers: What are the implications for consumers?'* – Consumers International – September 2012.

## EXAMPLES OF RECENT CONTROVERSIES AND COMPANIES' RESPONSIVENESS

- In January 2015, **Diageo** (part of European Beverage sector) was criticised by an interest group of small businesses in the UK for its decision of extending payment delays from 60 to 90 days for its suppliers. The Forum of Private Business (FPB) complained that the extension of the payment delay was unfair and damaging to small businesses. The organisation has also called British authorities to remove the company from the list of signatories of the **UK Prompt Payment Code** and alleged that big companies like Diageo are increasingly using their suppliers as a line of credit to protect their own cash flows, adding a burden for small businesses. Diageo said in a statement that it valued all its suppliers and looked to have "open and fair relationships" with them. Moreover, the Company emphasised that it had not changed the existing payment terms with its current suppliers (it will only apply to new contracts) and that the new financing programme would enable suppliers to benefit from early payment<sup>(31)</sup>.
- In February 2015, UK's Groceries Code Adjudicator (GCA) launched an investigation on **Tesco** (Supermarkets Europe) for suspected violations of its code, including several that linked to supplier relations (delayed payments to suppliers, delays in refunding suppliers when Tesco incorrectly issued duplicate invoices, imposing penalties when it claimed items were missing from deliveries). In response to this launched investigation, Tesco reported that the Company worked closely with the office of the adjudicator since its creation to put in place strong compliance processes. The Company also stated that it worked with the GCA to identify any relevant grocery Code issues and an internal review was carried out and shared with the GCA identified some areas of concern. As a result Tesco reported that it has taken action to strengthen compliance, is changing the way it works with suppliers and will continue to cooperate fully with the GCA welcoming the opportunity for Tesco's suppliers to provide direct feedback<sup>(32)</sup>.

<sup>(31)</sup> 'Diageo "threatens backbone of economy" by squeezing suppliers' – The Telegraph – 26/01/2015; "Broken big business ethics": Diageo attacked for extending supplier payment terms' – Food&DrinkEurope.com – 28/01/2015;

'Diageo attacked for 90-day supplier payments' – The Times – 28/01/2015; 'Diageo using finance scheme to cover poor payment practice says Forum' – Forum of Private Business Press Release – 27/01/2015

<sup>(32)</sup> "Supermarket watchdog investigates Tesco's deals with suppliers" – The Guardian – February 5th, 2015; "Tesco under investigation over suspected supplier mistreatment" – The Telegraph – February 5th, 2015; "Tesco investigated by new regulator" – BBC – February 5th, 2015; "Watchdog warns UK stores over Tesco probe" – Financial Times – February 5th, 2015

## ● Top 10 Company performances on sustainable relations with suppliers

Company	Country	Sector	Score (/100)	Overall CSR score (/100)	Market Cap. (EUR bn)
BIC	France	Specialised Retail	66	56	7.30
Sainsbury (J)	United Kingdom	Supermarkets	57	35	6.95
Olam International	Singapore	Food	56	29	3.32
Kingfisher	United Kingdom	Specialised Retail	52	53	11.90
Inditex	Spain	Specialised Retail	49	52	9.51
Rémy Cointreau	France	Beverage	49	43	3.24
Britvic	United Kingdom	Beverage	49	42	2.65
Kesko	Finland	Supermarkets	47	43	3.27
Hennes & Mauritz	Sweden	Specialised Retail	46	36	60.70
Ross Stores	United States	Specialised Retail	46	36	18.20

### KEY FINDINGS

- **The top 10 companies are diverse** in terms of their size and regional representation (representation from North America, Asia Pacific and Europe).
- One company, **BIC**, achieves an advanced score (66/100). The rest of the top 10 achieve limited to robust performances, ranging from 36/100 to 56/100.

### BEST PRACTICES

- **BIC** has issued a formalised commitment to establish sustainable relationships with its suppliers and subcontractors in its 'Purchasing Golden Rules'. This policy includes a commitment to Combating supplier's financial dependence; promoting long-term partnerships; prevent unreasonable or discriminatory trading terms or conditions. The company has allocated significant resources to manage sustainable relations with its suppliers, including risk maps on financial dependence, complaints management system for suppliers and offers suppliers' technical support as well as assistance and training.
- Two companies disclose positive and exhaustive key performance indicators:
  - **Olam**: income per farmer, premium per farmer and microfinance and crop financing have all increased between FY2012 to FY2013.
  - **Britvic**: average number of days of payments outstanding for the group have decreased over five years (2009-2013).

## CONCLUSION

- This study has emphasised the expectations, reflected in international reference texts (such as the UN Guiding Principles and the updated OECD guidelines), that companies should be managing social and environmental impacts even when these are not part of their own and direct operations.

The overall findings show that most industries still have a long way to go to demonstrate responsible supply chain management. This trend is revealed for all regions and all countries. Performance levels do not appear to be linked to a company's activities or a company's proximity to the final consumer. This indicates that although we live in a world with globalised production and consumption, we continue to see a very segmented world in terms of environmental and social standards. This imbalance is a persistent facet of globalisation.

- Of those companies that do report steps to tackle these challenges, there is currently more of a focus on *selecting and controlling* suppliers on social and environmental standards, rather than on developing fair and balanced relations with suppliers. This is despite the fact that the maintenance of balance and fair relations with suppliers can be a risk mitigation tool for companies. For instance, suppliers' economic viability can be enhanced by being paid on time and by receiving financial and technical support. This viability is then key for a business to avoid disruption to supplies and thus ensure continual operations. Such relations can also allow companies' to have better knowledge of the suppliers, which can lead to the identification of the social and environmental risks and even help them to progress towards the implementation of more sustainable approaches.
- When looking at specific practices, this study identified that there is also a central role that different stakeholders can play in strengthening social and environmental standards in supply chains. NGOs, for instance, have increasingly turned their attention towards business, in either confronting companies directly or seeking opportunities to collaborate. In addition, having free, independent and active employee representative organisations can ensure reliable and objective reporting and follow-up of concerns. Despite this, there is currently a lack of evidence that more than an isolated number of companies are seizing the reputational and operational opportunities that can be gained by working with key stakeholders.
- Finally, instead of 're-inventing the wheel', there is clearly much room to improve the current audit model. In fact, although audits were widely reported, companies often fail to provide comprehensive information on their scope, thus lowering the assurance that these audits cover key social and environmental topics. Alongside this, the vast majority of companies do not report that they have implemented corrective measures for any social or environmental incidents identified in their supply chains. This is a concern because a lack of follow up can completely undermine the utility of audits and any other measures installed.



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On December 15th, 2015, Vigeo’s Assembly of Shareholders endorsed the merger of these two established environmental, social and governance (ESG) research agencies from France and the United Kingdom, and the transaction was completed on December 22nd. Vigeo was founded in 2002 by Nicole Notat and EIRIS was created 32 years ago. Vigeo proceeded to raise 6.3 million euros of new capital to fund the EIRIS acquisition and to ensure that the new entity has the funds necessary for Vigeo Eiris’ future.

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