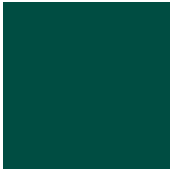




**Socially Responsible
Procurement:** Corporate Social
Responsibility in a supply chain context



CIPS Australia



Socially Responsible Procurement: An Introduction

Most people are now familiar with Corporate Social Responsibility (CSR) in some form or another – whether because of scandals over the use of sweatshops, or because employing organisations may have developed strategies to deal with issues such as ‘good corporate governance’ or ‘environmental responsibility.’

Internationally, CSR is an increasingly important issue that is being specifically and systematically addressed by many companies – large and small. This is why international companies feature most prominently on global sustainability registers, such as the Global 100 Most Sustainable Corporations in the World.¹

In broad terms, CSR is about corporate behaviour, governance and transparency in key social, environmental and business areas. It’s about considering the broader impact of company actions on all stakeholders. It’s about ensuring that companies do business responsibly, take a leadership position in community and social issues relevant to its own business operations (including those of its supply network), and are transparent about their actions in these areas.² ‘Triple bottom line reporting’ or ‘the triple bottom line’ says that a company needs to be responsible for not only its financial performance, but also its social and environmental performance.

Where CSR practices relate to procurement, CIPSA calls this “Socially Responsible Procurement” (SRP) - how best to achieve good social and environmental performance in the supply chain. A slightly newer concept to Australia, many of our own organisations (of various sizes) are beginning to realise the importance of addressing key SRP issues.

¹ www.global100.org - Insurance Australia Limited and Westpac Banking Corporation were the only Australian companies to rate in the Top 100. Westpac also recently ranked highest in the CRI Australia survey. The UK featured most prominently.

² ‘The Business Case for Productive Diversity and its Relationship to Corporate Sustainability’ – Paper prepared by Positive Outcomes for the Department of Immigration and Multicultural and Indigenous Affairs, March 2002.

“More than goodwill, corporate community involvement or strategic corporate philanthropy, corporate social responsibility is a genuine attempt by a company to build meaningful relationships between the corporate sector and the rest of society.”³

The plethora of issues that have arisen from the effects of globalisation are receiving increased social, media, and therefore political, attention. The CSR credentials of companies are being assessed by the media, regulators, the community, customers and shareholders, as well as by socially responsible investors considering their options. Business leaders are increasingly being expected to ensure that their companies behave as ‘good corporate citizens’, not only at home, but in their dealings internationally.

However, this means that business leaders face tough decisions, including how to balance the interests of shareholders, and their expectations of high returns, with CSR practices (and their focus on the broader good of the community).

In the supply chain context, procurement professionals must take SRP into account, along with other corporate considerations, such as ‘value for money’ and low cost sourcing, as well as consumer expectations of low prices.

From an Australian regulatory point of view, there isn’t necessarily much to compel Australian companies to always strike the balance in favour of CSR, if it means diminishing its responsibilities to its shareholders. While there is increased regulation in terms of certain practices that relate to CSR and SRP in Australia (including amending legislation relating to corporate governance and to better protect outworkers), there certainly isn’t specific legislation that compels a company to develop practices that systematically address CSR and SRP for its own sake.⁴

Doing more than the bare minimum that the law requires is down to ‘voluntary engagement’. Although there are those pushing for increased regulation, this doesn’t look likely in the immediate future - with recent pushes for company directors to take into account the ‘public interest’ failing to gain political momentum in Canberra.⁵ The Parliamentary Joint Committee on Corporations and Financial Services on Corporate Responsibility: Managing Risk and Creating Value Report was tabled in parliament in late June. The report recommended the continuing support of ‘voluntary engagement’ and the wide adoption of corporate responsibility, suggesting that mandatory approaches to regulating directors’ duties in Australia are not appropriate.⁶

In terms of voluntary measures, the ASX have Corporate Responsibility Guidelines.⁷ However these are largely focused on corporate governance issues – only one aspect of CSR and SRP.

³ Corporate Social Responsibility Index Australia website: www.corporate-responsibility.com.au

⁴ For multinational Australian companies, however, CSR and SRP become more relevant because of greater regulation and emphasis internationally, for example, by the US Securities and Exchange Commission.

⁵ ‘Public interest calls for greater self regulation’, Tom Burton, The Age, CRI Special Report, page 3.

⁶ To view the report, go to: http://wopared.parl.net/senate/committee/corporations_ctte/corporate_responsibility/report/index.htm

⁷ The ASX Principles of Good Corporate Governance and Best Practice Recommendations are ten core principles relating to Corporate Governance, particularly directors’ duties.

There are also the OECD Guidelines for Multinational Enterprises - which include voluntary recommendations pertaining to many areas relating to CSR and SRP, such as human rights and the environment, and globally there are indexes like the FTSE Good Index series⁸ that assess companies on a variety of CSR criteria.

Another voluntary exercise, the third annual Corporate Responsibility Index, was recently published. It assessed 29 Australian companies and multinationals (including BHP Billiton, Amcor and Westpac) against social responsibility criteria, including labour rights in the supply chain. And while participation in this year's survey was up (from 27 to 29) and the quality of the rating scores was up, the participation level is hardly as large as it could be (in light of the fact that hundreds of companies are invited to participate) and the results also seem to indicate that many Australian companies 'talk' about their commitment to CSR more than they actually implement it.⁹

Interestingly for the procurement profession, "marketplace" issues were the second top scoring area of a company's performance (after workplace issues) - with performances in "the social stewardship of products and services" as well as "social supply chain management" scoring highest.¹⁰

The existence of the survey perhaps reflects a broader trend that several Australian companies are choosing to address CSR and SRP - either because they really want to or because they recognise the need to ensure a good reputation in the community and amongst potential and current shareholders. Whether many more will begin to participate in a voluntary survey that may embarrass them is another issue altogether.

Another factor in the rise of CSR and SRP is the fact that the behaviour of large companies is increasingly being driven by 'intangibles'. Business valuations are no longer based on just financials. Over 65% of drivers are now intangible and CSR cuts across quite a few of them. This includes: organisational reputation and brands; employee, supplier and distribution know-how; statement of goals; ethics and values; and the value of a company's public support base. This then adds a financial incentive for companies to integrate CSR and SRP into their practices.

SRP is also a potential opportunity for companies to work with their suppliers, for example, to "...identify new energy sources, new power sources for vehicles and an increasing emphasis on minimal environmental footprints,"¹¹ and to ensure that they move forward with more confidence in potentially risky areas such as low-cost off-shore sourcing (which raises key SRP issues such as bonded labour, child labour and corruption).

However, addressing SRP is not just about reputation, regulation, risk or opportunity. CIPSA believe that SRP is important and valuable for its own sake.

⁸ The FTSE4Good Index Series has been designed to measure the performance of companies that meet globally recognised corporate responsibility standards, and to facilitate investment in those companies. See: www.ftse.com (Indices section).

⁹ CRI Special Report: Corporate Responsibility Index, The Age, Monday May 15 2006.

¹⁰ Corporate Responsibility Index 2006, Executive Summary, page 3.

¹¹ CIPSA Practice Guide: CSR

The Elements of SRP

While Enron is an example of a major collapse in corporate governance, many CSR issues and risks actually emanate from the supply chain: child labour issues, sweatshop accusations and poor management practices. Therefore, in order to comply with CSR more generally, the external supply chain needs to be addressed. That's where SRP comes in.

The following elements of CSR are some of the most relevant to the various stakeholders involved in the supply chain, namely: employees, customers, suppliers, the community, the environment, staff, customers and shareholders. They therefore make up most of the elements of SRP:

Environmental Responsibility

As knowledge relating to environmental damage increases, the pressure to change the ways in which organisations behave has increased – particularly amongst the manufacturing, mining and resources sectors. Companies need to monitor the environmental impact of suppliers, and develop an environmental purchasing policy that aims to reduce the environmental impact of their own and their suppliers' activities, goods and services (otherwise known as 'green buying').

Human Rights

Human rights in the supply chain includes a range of complex issues, such as: slavery, bonded labour, child labour, freedom of association, working conditions and wages, exploitation and non-discrimination.

Equal Opportunity

Equal Opportunity addresses acts of discrimination on the basis of race, sex, religion, sexual orientation, disability and age.

Diversity

As a concept 'supplier diversity' is often mistakenly taken to mean any initiative to broaden an organisation's supply base, for example by increasing the number of suppliers with whom the organisation does business. However, supplier diversity actually refers to initiatives that aim to increase the number of diversely controlled (e.g. ethnic-minority owned or women-owned) businesses that supply goods and services to both public and private sector organisations.¹² It's about creating a level playing field, by offering under-represented businesses the same opportunities to compete for the supply of quality goods and services, as other qualified suppliers. Positive discrimination even.

*"By increasing the diversity of our workforce, sales organisations and supplier communities we improve our access to people with talent and become more aware of our customers' needs, which enables us to create valued products and services."*¹³

Corporate Governance

Supply chain governance is an integral aspect of the overall corporate governance of an organisation. It requires strong and transparent reporting processes across supply networks and supplier accountability for supplier performance.

¹² Ram and Smallbone.

¹³ 'Diversity is Everybody's Business Project' Volvo Car Corporation August 2001, page 4.



Sustainability

Sustainability is about living and working in ways that meet and integrate existing environmental, economic and social needs without compromising the well-being of future generations.¹⁴ Obviously this is particularly significant for the supply chain, which can make a significant contribution to sustainable development, resource minimisation and risk minimisation. “Put back what you’ve taken out” is becoming a SRP philosophy. This is increasingly the case in the Australian resource sector, as an example.

Impact on Society

The approach an organisation takes to labour and supplier relations can determine whether or not they are seen as a ‘good corporate citizen’ or a ‘good employer’.

Ethics & Ethical Trading

Businesses are increasingly doing business in a ‘borderless’ world, which makes it even more essential to develop core principles of conduct, which can then be applied to employees and suppliers worldwide – morally if not legally.

Biodiversity

Biodiversity relates to protecting diversity concerning habitat, genetics and species and, as such, has an obvious impact on SRP – particularly offshore suppliers in developing nations.

Community Involvement

Companies that engage and assist their communities become valuable members of those communities and more respected by their stakeholder.

¹⁴ The Sustainability Report: <http://www.sustreport.org/>

Why SRP? The CIPS Position

- CIPSA understands that CSR has become the broadly accepted phrase to describe a collection of interrelated disciplines all of which combine to represent an organisation's overall ethos, its personality, philosophy and character, in relation to its role in the world in the largest sense.
- CIPSA believes that CSR and SRP are both simply good business practices. They embrace how organisations are run and their commitment to all stakeholders, in particular and increasingly to customers who are demanding that their suppliers be environmentally sound.
- CIPSA believes that sound SRP practises will have a payback to all stakeholders and is therefore in the best long-term interest of the organisation.
- CIPSA encourages procurement professionals to consider the long-term consequences of their actions and to question objectives that may unintentionally have negative socio-economic repercussions.
- CIPSA believes that procurement professionals should play an integral role in influencing board directors to affect the desired company position relating to SRP.
- CIPSA believes that procurement professionals should adopt a 'balanced scorecard' approach when assessing SRP credentials which would bring with it an inherent logic that would ensure adequate consideration is given to the interrelated elements of SRP.
- CIPSA believes that the procurement function is the most appropriate place from which to manage all aspects of SRP.

Implementation Tip

A 'balanced scorecard' approach to assessing suppliers can determine and weigh relevant factors alongside the elements of SRP, such as: financial stability, technology, commercial performance, delivery capability and quality management – and assess these factors not only according to current performance, but on the existence of processes that make sustaining that performance likely into the future*.

*For more information on the balanced scorecard approach, please visit: www.niwotridge.com/Resources/DomainLinks/BalancedScoreCard.htm

SRP in Australia: Emerging Issues and Trends

The Australian procurement environment involves buying locally in a well-developed economy and regulatory environment. Therefore, we don't necessarily see the full range of SRP concerns that emerge within the rest of the world. However, that doesn't mean that vigilance is not required.

Australia's borders are relatively secure, and do not have some of the illegal immigrant labour issues that are prominent in countries like the USA. However, there has been some recent media attention about the working conditions of migrant workers, and an alleged overuse of 'Type 457' visas in order to access a cheap workforce.¹⁵ And while there aren't racial reporting requirements like the USA, there are those who feel that treatment of the indigenous population is becoming an important SRP issue in Australia (particularly in the mining sector).¹⁶

Other key issues that will continue to emerge in Australia are environmental issues such as climate change, emissions control, water shortage and fuel consumption. What do we do about suppliers that use a large amount of water in their manufacturing processes? What about those who use coal and oil, which aren't sustainable?

Some companies seem to be taking a lead. Boral, for example, has implemented strategies to reduce its fuel consumption and greenhouse gas emissions relating to the transportation of its materials, and has implemented an online sustainability reporting tool.¹⁷ Orica too, have a range of sustainability policies (including a policy to "sell only those products that can be produced, transported, stored, used and disposed of safely."¹⁸), and have publicly available searchable data on their performance. The company has implemented the 'Natural Step' program for product development. This program, based on international scientific research, helps the company identify how it can assist its suppliers improve their environmental performance.¹⁹

From an Australian SRP perspective, it's really once companies go off-shore in search of suppliers that SRP considerations arise in a more systematic way, particularly in relation to human rights, remuneration, safety and working conditions. Areas where Australian domestic legal requirements are comprehensive.

¹⁵ The 7.30 Report on the ABC, 18 May 2006, featured a report about Korean migrant workers complaining about not being paid appropriately and not receiving promised health cover.

¹⁶ 'Power to the People' by Vickie Smiles, The Age, CRI Special Report, May 15 2006, page 4.

¹⁷ 'Built to last for future generations', Vickie Smiles, The Age, CRI Special Report, May 15 2006, page 4. Boral has replaced 50% of its fossil fuel use with alternative fuel sources, such as used tyres and tallow residue, for example.

¹⁸ See: www.orica.com.au: SH&E section.

¹⁹ See Natural Step website at: http://www.naturalstep.org/com/TNS_for_business/

Implementing SRP

“To be considered effective, corporate social responsibility must be an integrated part of day-to-day business, engaging all stakeholders, and including strategies to support individual managers to make socially responsible decisions, conform to ethical behaviour and obey the law.”²⁰

Implementation Tips

- Link with the organisation’s overall CSR policy and exert influence on its approach from the supply-side/SRP perspective.
- Ensure the sourcing strategy delivers what the organisation as a whole is aiming for and its commitments are entirely practicable within existing policies (such as value for money or cost reduction).
- Identify the most relevant SRP practices for your specific organisation.
- Get high-level corporate buy-in for your SRP policies and communicate this to the supply chain.
- Review products/services/suppliers for potential benefits and risks from SRP impact and identify the likelihood and potential impact of risk/reward from each.
- Prioritise analysis and action on higher risk/reward areas and check the likely impact throughout the supply chain.
- Balance the SRP impact within the organisation’s overall sourcing strategy.
- Work with suppliers, where possible, to improve their SRP performance.
- No two organisations will have exactly the same requirements, and therefore a unique ‘risk/rank’ model will need to be developed that encompasses social, environmental and economic risks.
- Communicate your SRP policies openly eg: on your website

Implementation of SRP can be divided into four stages:

1. Driving forces and key issues
2. Prioritisation
3. Supply chain communication
4. Operational processes

²⁰ Corporate Social Responsibility Index Australia: www.corporate-responsibility.com.au

1. Driving forces and key issues

In order to successfully implement SRP, what drives SRP and how these drivers are prioritised within the organisation need to be considered:

- The value set of the community in which you operate
- The internal values of your organisation
- Managing risk within the organisation

Each organisation will prioritise these differently. Once these drivers are considered, it's about focussing down to the key SRP issues that could affect a specific supply chain.

The development of an SRP policy, such as a 'supplier code of behaviour' or 'ethical sourcing standards' (ESS) is an important exercise during this phase of implementation.

Key Enablers to SRP

- Leadership
- Technology and information systems
- Comprehensive database of supply base (right down to manufacturing sites)
- Audits that don't fatigue your supply base
- Adequate resources
- Making SRP a natural part of decision-making
- Building SRP into your supply chain culture

2. Prioritisation

When thinking about actually implementing SRP, the temptation may be to stay at the high level. However, to successfully address SRP, it needs to be taken right down to the product level. This essentially involves 'deconstructing' your supply chain: starting in areas of significant or strategic spend, identifying the 'products' (goods or services) that are purchased, mapping the supply chain for each of these 'products' and looking for any potential SRP impacts. This process can then be applied to the rest of your spend areas.

The way of doing this will depend on the SRP drivers mentioned in point 1 above, but for most a 'risk' focus would be appropriate. A risk analysis involves:

- Mapping the supply chain (A key issue here becomes "how far down the supply chain should I go?")
- Identifying the potential SRP risks involved with each supplier within the supply chain (this includes knowledge of the supplier's local labour laws and practices)
- Prioritising the SRP risks from 'low' to 'medium' to 'high'
- Prioritising the business impact of each product from 'low' to 'medium' to 'high' (in terms of key factors such as whether the product is a key input)

to the manufacturing process or perhaps has an important association with one of your brands)

Figure 1, on page 12, illustrates this process.

A mitigation plan should then be developed for the suppliers of those 'products' that rank highly in both SRP risk and business impact. The mitigation plan should commence with an investigation to confirm whether the identified SRP risk really is an issue. If so, what are the options? Do you need to look for an alternate source of supply, or can you help to improve that supplier's practices by working together with that supplier to decrease the SRP risk? For more complex or larger scale SRP issues that effect entire supply markets, it may be necessary to organise and/or participate in 'industry led' forums such as industry roundtables where all participants in the supply market (buyers, sellers, and possibly NGO's and government) collaborate to manage the SRP issues. The 'Palm Oil Roundtable for Sustainability' is an example of an industry led forum that has been established in order to help palm oil suppliers address SRP concerns with cash cropping in South East Asia.

Identified SRP risks should then be 'graded' or categorised. One method of categorisation is the 'traffic light' approach:

- **Red:** Send the issue to higher management level.
- **Amber:** The issue is significant, but can be solved locally.
- **Green:** Action plan is in place to resolve the issue.

3. Supply chain communication

Once your suppliers have been analysed and the issues categorised, the next step is to determine how these suppliers are going to be managed and communicated with as part of your SRP management process. This element of SRP is essential. Many organisations may have developed a SRP policy, but how that has been enforced is a key consideration.

For example:

High-risk suppliers: Direct dialogue involving a face-to-face meeting would be required with these suppliers in order to engage in dialogue.

Medium-risk suppliers: These suppliers would need to be actively engaged on SRP issues. For example, each supplier could be requested to demonstrate its adherence to the ESS via some form of reporting system.

Low-risk suppliers: Passive communication of SRP requirements only, via standard terms and conditions on purchase orders, for example.

Many companies are using online technologies to communicate with and monitor their supply chain.²¹ There are various online reporting technologies that allow suppliers to enter the method by which they are complying with the ESS. An emerging issue here may be one of supplier fatigue: whose standards should a supplier comply with?

²¹ One such initiative is an online reporting tool called SEDEX, which allows suppliers to log on and enter information against compliance standards. Companies can receive supplier 'scores', based on their own criteria.

4. Operational processes

So how can all of this analysis be built into the operational processes? There are cost reduction goals to meet and you have to source ethically and sustainably as well? How can you measure and demonstrate this? What are the KPIs?

There is no doubting that tangibly measuring SRP is definitely a key challenge. One way to do so is to try and put some sort of metrics in place (for example: “100% of the ‘high risk’ suppliers to be SRP compliant by 2007”) and to build the SRP requirements into the performance objectives for suppliers.

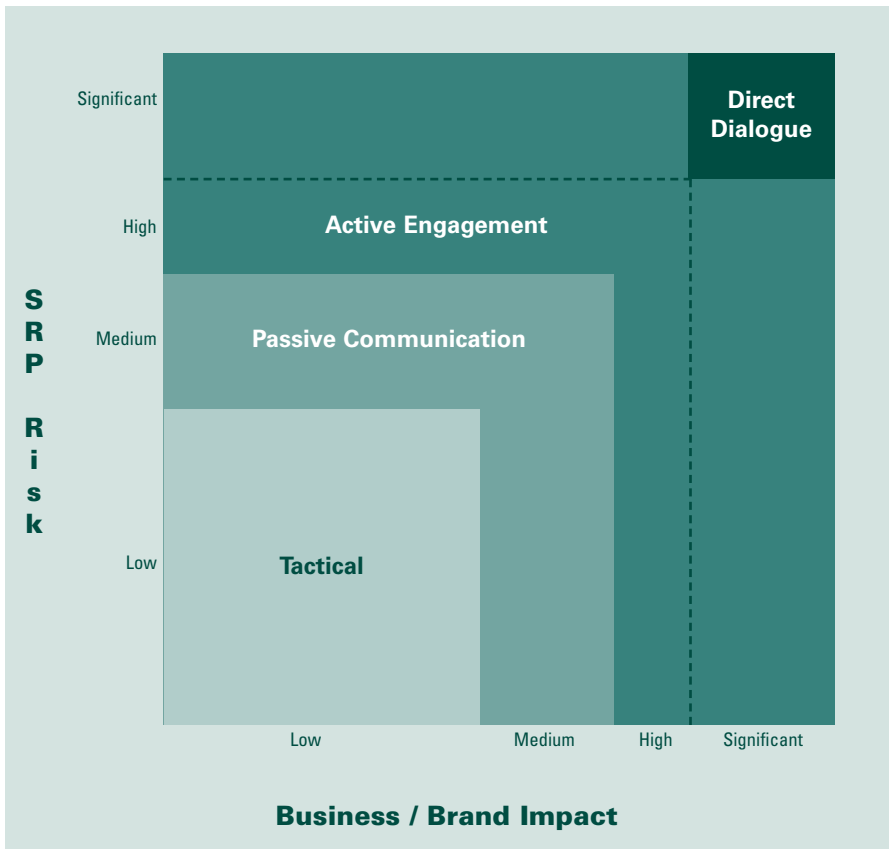


Figure 1: A Risk-based approach to assessing SRP in the supply chain. Source: Adapted from CIPS UK model

Where to now?

Regulation of SRP will most likely continue to evolve, with a trend towards global agreement and standards (such as is occurring with the recent USA-Australia Free Trade Agreement and the Kyoto Protocol, the International Labour Organisation, the Global Compact and work being conducted on the UN Norms). In terms of domestic legislation though, for now at least, it would seem that the procurement industry will be left to raise the bar of its own accord.

In the wider business context, however, there is a clear trend towards organisations accepting that it is in their own long-term best interests to accept and afford a firmer approach to CSR right now.

Useful Resources

Publications:

CIPS CSR White Paper

CIPS Principles on CSR

CIPS Briefing on Supplier Diversity

CIPS Practice Guide on Supplier Diversity

CIPS Practice Guide on CSR Codes and Standards

CIPS Practice Guide on Sustainability

CIPS Practice Guide on the Environment

CIPS Insight Guide on CSR 'The Ethical Decision'

CIPS Insight Guide on Corporate Social Leadership

CIPS Insight Guide on Human Rights

CIPS Insight Guide on Supply Chain Governance

Parliamentary Joint Committee on Corporations and Financial Services on Corporate Responsibility: Managing Risk and Creating Value

Websites:

ASX Corporate Governance Guidelines:
www.asx.com.au/about/pdf/ASXRecommendations.pdf

Dow Jones Sustainability Indexes:
www.sustainability-indexes.com

FTSE4GoodIndex series:
www.ftse.com/Indices/index.jsp

Sustainability Reports for Multinational Companies:
www.sustainability-reports.com

The Corporate Responsibility Index:
www.corporate-responsibility.com.au

The Global 100 Most Sustainable Corporations in the World: www.global100.org

The OECD Guidelines for Multinational Enterprises:
www.oecd.org

The Sustainability Report: www.sustreport.org

World Council for Sustainable Development:
www.wbcsd.org

About the Author, Acknowledgement

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