



Ethical Sourcing Report North America 2008



**WHAT NEW
INITIATIVES
ARE SHAPING
THE FUTURE
OF THE
ETHICAL
SOURCING
DEBATE?**

INSIDE

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Working With Suppliers and Co-operating with Competitors

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ETHICAL SOURCING REPORT NORTH AMERICA 2008

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EXECUTIVE SUMMARY

This issue of *Ethical Sourcing Report* seeks to address some of the major issues facing supply chain professionals, focusing on examples of best practice while highlighting concerns and problems.

Firstly, from page 4 we ask three industry experts to share their views on what they are optimistic about, and which initiatives they applaud. Then from page 10 we address how to measure the success of supply chain and ethical sourcing initiatives – many brands and companies now have good programmes in place, but they are only going to continue if their success is clear and demonstrable.

Forced and child labour in supply chains has, rightly, attracted the most negative publicity for many brands. And while engaging with supplier factories is a challenge, it is even more difficult to be certain where raw materials are coming from. A prime example is the cotton sector, particularly in relation to the central Asian republic of Uzbekistan, and we explain the issues from page 13.

Developing long-term relationships with suppliers is an effective method of ensuring corporate values filter down the chain. From page 15, we case study how Starbucks has taken the long-term view. And also examine the value of cross-industry co-operation initiatives from page 18 – taking Levi Strauss and HP as examples – and ask if sharing data and information really can save everyone time and resources.

With accusations of “greenwash” flying around it is important to be confident when you are sourcing environmentally-sustainable products. From page 22 we explain what to watch out for. And finally, from page 26, we ask a local expert to explain how to tackle China's environmental rules and regulations – vitally important for any brand sourcing or planning to source from the country.



INDUSTRY TAKES THE LEAD FOR ETHICAL SOURCING

What are the new initiatives that are taking the ethical sourcing debate forward and continuing to develop supply chain best practice? *Ethical Sourcing Report* has asked three experts – consultant **Doug Cahn**, the Fair Labor Association’s **Auret van Heerden** and PVH’s **Marcela Manubens** – to outline what is giving them cause for optimism, what things are still getting in the way of progress and the key attributes that are required for successful collaboration and co-operation.

Developing awareness

A “growing awareness of CSR’s requirements in producer countries” is something that Doug Cahn highlights as a recent positive development, particularly where there is a developing culture of change. Along with this, “more robust collaboration in the buyer community” is increasing. “We have sector-wide initiatives that are building on the work in the past when some pioneers were working on their own,” Cahn says. And with collaboration comes “increasing leverage in supply chains, building efficiency into systems”.

Capacity building at factories is another factor Cahn stresses. “There’s now a focus away from ‘traditional’ monitoring, with tools being developed that allow for compliance. There are more opportunities for training – but these do need to be in place for there to be sustained progress.”

In terms of ongoing major problems the industry still faces, Cahn picks out the “rampant and ongoing falsification of records.” While checking for such things is a routine part of any assessment process, “the fact that there is a lack of transparency means that it is difficult to have an honest conversation”. Primarily, Cahn argues: “This continues to be a persistent attribute surrounding records of hours and wages, with employees under-compensated for hours worked. It’s a core problem.”

Price pressure and unrealistic expectations from buyers are also negative factors in the overall ethical sourcing debate. Cahn says: “Expecting fast times from factory to market, and heavy incidence of late ordering are an everyday part of the job for brands and retailers.” But this puts the pressure on factory management to bend the rules to meet their

customers' expectations. "The model poses a number of dilemmas" for factories.

And while there is an increasing level of consumer awareness of the issues, and a corresponding greater demand for ethically sourced goods, "they are not yet engaged to the extent that would provide brands with a mandate to alter existing business models".

"Informal networks and conversations are moving on to becoming more established codes and organisations"

Doug Cahn

The number of collaborative initiatives that have developed encourages Cahn. "There is a lot of promise in some of the things that are going on. Informal networks and conversations are moving on to becoming more established codes and organisations. CSR executives are getting together and sharing information." He picks out in particular the International Labour Organization for moving the debate forward effectively, and the Fair Factories Clearinghouse (see box on p6), an initiative with which Cahn has been closely involved.

Lip service

Despite positive moves, however, Cahn says that there is still too much "lip service" to dealing with problems at a worker level. "There needs to be better communication with workers, and trust is absolutely essential. And trust happens when there is transparency. Workers need to feel that their concerns are respected and being addressed and for this there needs to be a system of dialogue with factory management, and responsiveness from them." While "workers are not going to get everything they want", the most important thing is for there to be a process with results.

And to get factory management buy-in to improving conditions, there are two key approaches Cahn highlights. Firstly, if there is collaboration among the brands or buyers at a particular factory, and they then co-ordinate on what they ask of the factory in terms of improvements and worker conditions, it is much easier for the factory to be able to get on with the remediation required. Secondly, there is significant efficiency in costs for factories in co-operating with brands collectively. Fewer audits doesn't just mean

savings for the brands: it's great news for factories too as they can concentrate resources on implementing improvements (and, of course, producing the products they are in business to make in the first place).

For brands themselves, reputation is such a major concern that it's in the interests of all to ensure that their sector, as a whole, remains untarnished. Poor practice in a factory hurts everyone "whether or not it's your particular brand that's under the spotlight at any one time". The answer is to work together and ensure that, sector-wide, practices that attract the really damaging negative publicity are eliminated.



Doug Cahn has 30 years of experience as a corporate responsibility professional. Formerly head of human rights programmes at Reebok International, he is currently chairman of the Fair Factories Clearinghouse, president of Clear Voice, an independent and confidential communication channel for workers, and principal of The Cahn Group consultancy.

Beyond monitoring

Auret van Heerden, president and CEO of the Fair Labor Association, says that the debate now has moved beyond monitoring. "The fact that there are thousands of codes of conduct, and that companies are looking at social audit and compliance issues has been a giant first step. But while audits are great at identifying the issues, there is not so much clarity on suggesting the changes required. So we are getting to the 'beyond the audit' stage."

Also positive is the fact that suppliers are taking the initiative. Van Heerden says: "The management at some factories are saying 'let us take ownership of the issues' and get their factories up to standards so that they can pass any audit."

"Tailor-made capacity building on a factory-by-factory basis can be an effective solution"

Auret van Heerden

Standing in the way of such an approach, however, can be intransigence on the part of buyers that insist factories have to follow their brand's procedures, whatever the standards currently in place. "Bureaucratic procedures at the buyer level can be a very blunt instrument," van Heerden argues.

He says that a more effective approach is to deal with factories on an individual basis. "Tailor-made capacity building on a factory-by-factory basis can be an effective solution." Of course, this requires factories to be candid about their procedures – something that van Heerden admits can take a number of meetings to achieve. "Another problem is that many buyers are suspicious and worry that factories will try to cheat the process. At the FLA, we find ourselves having to argue the case for giving them at least a chance,

demonstrating that some suppliers do want to engage in the process."

It is still difficult, van Heerden says, to get co-ordination between companies that are auditing, with "too much going round in circles". To achieve effective change, there needs to be commitment on all sides to remediation measures. An awareness that the process "takes time" is vital.

FAIR FACTORIES CLEARINGHOUSE: SHARING DATA FOR MUTUAL SUCCESS

The FFC is dedicated to improving the availability of factory-compliance audits, by providing its members with the use of a compliance data management system that stores, manages, and tracks workplace conditions. The system also facilitates the exchange of non-competitive information concerning factory compliance between brands and retailers, and so aims to reduce audit fatigue for factories.

Marychris Melli, FFC programme director, says that through the use of its tools the organisation "seeks to help companies make informed decisions about their sourcing, and to facilitate improved processes for addressing supply chain compliance". FFC's recently-launched Sharing Platform is a tool that allows companies to contribute to FFC's factories database, search for factories shared with other FFC members, share appropriate factory compliance information, and initiate collaboration on auditing, remediation and corrective action plans. The Sharing Platform complements FFC's Compliance Data Management System, which enables all aspects of auditing, management of supply chain and sourcing information, and customised reporting on all data including remediation measures and corrective action plans.

While arguing that many companies are getting involved in data sharing for "altruistic reasons" Melli says there are also cost benefits to be realised in compliance programmes if audit duplication is avoided. "If there is even a 10% to 15% overlap rate, this can provide a company the ability to reallocate compliance resources to address areas that can provide more sustainable benefits for suppliers such as root cause identification of compliance issues or the institution of formal training programmes." In addition, with the ability to identify potential compliance issues before visiting a supplier, companies can conduct more focused audits and potentially help to facilitate transparency on the part of the factory.

For more information go to www.fairfactories.org

Accountability

Increasingly, it is the accountability debate that is driving best practice. Van Heerden picks up something mentioned by UN special representative for human rights John Ruggie: thousands of companies may be responsible, but very few are actually accountable. In other words, there are not many companies that are really "grappling with what it all means".

"What gets measured gets done" may be a bit of an old cliché, but van Heerden says that in this case it holds true. "The best companies are putting in metrics, setting challenging targets and then assessing progress against them." Many brands may have "learnt the hard way" with negative publicity from exposures of bad labour practices at supplier factories. But some of these "have become best in class" and made enormous progress.

Van Heerden says: "The most socially responsible companies don't claim to have all the answers. But the public can have trust in them now as they are raising the bar." As an example of where brands are leading the debate, even taking the place of government in improving standards, van Heerden points to Bangladesh. The minimum wage in the country had been painfully inadequate since the 1990s, and prompted riots in 2005 when the decrease in real terms pay had reached a crisis point. "The government was slow to react, but brands went and met with ministers to try and get the situation resolved." A revised wage rate was agreed, but even then it was down to "the leading international buyers who had to insist it was paid". So it was brands that were pushing the agenda.

The leading buyers are now "getting beyond the checklist approach," van Heerden believes, and he argues that developing systems of key performance indicators (KPIs) is the next step. "Take employee grievance procedures. If you can put in place some KPIs that examine, for example, how many grievances a factory has had, what they were about, how long they took to resolve and how many resolutions



were accepted by all parties, then immediately you can have a good look at the health of the factory.” These numbers can be correlated with labour turnover figures. And, clearly, improvements can be more easily monitored.



Aurret van Heerden has over 30 years’ experience in international human and labour rights. He began campaigning for worker rights as a student in apartheid South Africa and served two terms as president of the National Union of South African Students. After a period in forced exile, during which he worked for the ILO in Geneva, he was appointed by the new South African government to be labour attaché at the UN. Subsequently he returned to the ILO, before setting up the European subsidiary of the FLA in Geneva, where he is now president and CEO.

Getting mainstream

Marcela Manubens, senior vice-president for global human rights and social responsibility programmes at the Phillips-Van Heusen Corporation, says she is very positive about ethical sourcing, and the associated corporate values, becoming more mainstream business practice.

She is enthusiastic about the numbers of “values-oriented” graduates coming out of colleges and universities. “They want to exercise their spending power in a good way and want to work for companies where CSR is embedded,” she says. This means, if nothing else, that “there will be more executives with values in the future”.

Manubens also picks out a more positive relationship with NGOs as further cause for optimism. “There was a bit of a ‘catch-you’ attitude from some civil society NGOs in the past, who seemed to believe that all companies were evil, while many companies regarded NGOs as extremists.” Not so now, particularly among leading companies, Manubens argues, which is indicative of “how far we have come” and to a lot of hard work from all sides keen to develop ways of working together effectively. She says that the engagement of civil society groups and corporations “in constructive dialogue brings a better understanding of the issues, cohesive efforts to improve conditions and innovative thinking to find win-win solutions”. And, more than that, “it helps build trust”.

Measuring company performance by triple-bottom-line assessment is how the value of corporate social and environmental performance can be integrated into business models, Manubens says. And when the financial community realises that the profitable companies will be the ones integrating sustainable practices, corporate social responsibility will then be embedded in standard company economics.

Making the business case is more difficult in times of economic slowdown or potential recession. When consumers have less money to spend, “how you manufacture and price your products becomes even more important,” Manubens says. Inevitably there is a renewed focus on price as a key driver on purchasing decisions.

But engaging with consumers, economic downturn or not, is a key issue, she believes. “Simple economics suggests the sustainability of CSR/ethical sourcing depends on consumers

being on board and rewarding ethical companies with their purchases. While campaigning and targeting companies prompts action from responsible corporations, it doesn't guarantee the sustainability of the ethical sourcing model." Manubens argues that values-driven consumers who reward brands with their purchases will in fact have an important role in this sustainability.

"Values-oriented graduates want to work for companies where CSR is embedded"

Marcela Manubens

There is a lot that companies can do right now, however, and Manubens agrees that cross-sector collaboration is one area where there have been major improvements particularly where there is "co-operation to reduce duplication of work". She says: "There are so many issues that can't be solved by one company acting alone. Good initiatives are the ones that target the endemic problems, and deal with, for example, capacity building and engaging with supplier management." So, there is a bigger picture emerging for the future of corporate responsibility and ethics that ties together the growth of SRI, and the fact that pension companies are now wanting to invest in ethical funds, with the growing band of ethically-aware professionals in positions of power at leading brands.

And given that ethical sourcing and supply chain management are in essence just doing the right thing, this is a trend that is likely to continue.



Marcela Manubens has created and now directs the human rights, working conditions and ethical sourcing efforts for Phillips-Van Heusen in her role as senior vice-president of global human rights and the social responsibility programme. She has been an active participant in the FLA since 1996. Elected as a board member of the Fair Factories Clearinghouse, she heads its audit committee.



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MEASURING SUCCESS

As many companies are implementing new and innovative corporate responsibility programmes, particularly in their supply chains, the question now is how to measure their success. **Donna Chung** explains the importance of having measurement systems built into corporate ethics initiatives.

Q: It can be difficult to establish the success of ethical supply chain measures. What is your initial advice to companies facing this problem?

A: As a starting point, I think it's important, first of all, to not assume that existing programmes are successful. Companies should critically examine them, instead, and address the question: what measurable impact are ethical sourcing programmes (or other CSR initiatives) truly having?

It may be – and one certainly hopes – that current systems of internal and external supply chain monitoring (or other CSR measures) are having a positive impact, increasing factory-level compliance, protecting rights, and making working conditions safer and better for workers. But without proper systems of measurement, it's not possible to document those results and to even contemplate making improvement

on current systems. It may also be that the success of current practices is being under-reported, or under-appreciated, because of this lack of systematic assessment.

My advice to companies would be to, first, review and assess the current procedures to see whether they are designed to measure impact.

“Most companies have not set up their procedures to actually measure impact” Donna Chung

From what I can see, most companies have not set up their procedures to actually measure impact. Some critical questions, therefore, must be asked. Have you defined exactly what you're measuring? Have the appropriate indicators been

selected? Is your system set up to monitor these indicators on a regular basis? Are the data analysed appropriately? And, finally, does the analysis inform your future decisions on supply-chain management?

When linked with key performance indicators (KPIs), I believe the impact of CSR (or social compliance) programmes can be assessed in the most cost effective manner.

Q: In general terms, what are the method-types that can be used to gauge impact of CSR measures?

A: In general, it would be ideal if randomised evaluations could be set up, so that one would compare the outcomes observed in programme participants (factory workers, for instance) with those of “equivalent” persons not exposed to the programme. But there are many challenges to setting up such evaluations. For example, a company’s supplier factories are likely to be based in vastly different contexts, so that it may be difficult to establish “control” and “test” groups. Plus ethical questions arise in implementing what is hoped to be an “ethical” CSR measure in only a select group of factories.

Q: Given that there are no “control groups”, is it possible to estimate how things might have developed without a programme, so that the difference between actual outcomes and probable outcomes can be made clear?

A: Yes, there are tools that can be used to statistically control for the differences between groups that would otherwise lead to biased programme effect estimates.

Some popular statistical tools for this sort of analysis are: multivariate analysis; regression-discontinuity designs; and time-series designs. I personally like time-series designs, because they do not involve selection of different groups for comparison and tend to be simpler to design and implement.

Q: What sorts of systems should be implemented for projects so that their impact can be established?

A: There is unfortunately no straightforward answer to this.

The sort of “system” that might be best for a company

would depend largely on what ethical sourcing measures a company has in place and what “impact” the company wants to achieve through those measures. Once the causal links have been identified – the links between the CSR measures and their intended effects – then one must examine the assumptions underlying those links and test the causal links.

The method adopted to test the links would depend on many factors, including cost, timeline, commitment, level of co-operation of other stakeholders, etc.

Q: What is the importance of proximal and distal effects, and how are they related?

A: “Proximal effects” are those outcomes that are the immediate results of a programme. For example, one proximal effect of conducting a training programme on protective equipment in a factory for workers may be increased knowledge of how to use the equipment among the trained workers. One might measure this by having the participants take tests before and after the training, or to test the knowledge of participants against non-participants of otherwise equivalent make-up.

“Distal effects” are outcomes that are the ultimate intended results of a programme, which follow from the programme’s proximal effects. For example, a distal effect of the training programme may be that increased knowledge of how to use the protective gear leads to an increased usage of the protective equipment, so that a change in knowledge-level leads to a behavioural change. Or, the ultimate outcome intended, the distal effect of interest may be whether an increase in the use of the protective equipment has a corresponding effect of a decrease in the number of injuries in the relevant departments or factory lines using that safety gear.

It is important to identify the different levels of outcomes that can be measured. A correctly implemented impact assessment would express programme results as a logically-linked series of proximal and distal effects.

Q: Can you give any examples of projects where better measurement of outcomes has led to further success?

A: Unfortunately, in my experience of looking at companies in the past decade, I have not come across many examples of good practice in this area. A lot of the development of ethical

sourcing measures in the past 15 years has been “reactionary”, with companies adopting “policing” methods of testing and re-testing their supplier factories.

“Unless companies start to measure the impact of their CSR programmes effectively, the future of the whole CSR movement could come into question”

Donna Chung

Now, much emphasis is being placed on remediation measures and factory capacity building. But, unfortunately, most of these efforts are being made without the systematic integration of impact measurement.

I can think of one pilot project that was conducted in a few factories in China, where impact assessments were done on a small scale, measuring the impact of a “worker empowerment” and factory capacity building CSR programme. But that project, too, had some methodological weaknesses.

In general, companies’ programmes are not set up to measure impact reliably. Success of programmes often is couched in terms of dollars spent; or simple before-and-after snapshots are taken to mean “impact”. I think this is alarming, because unless companies start to measure the impact of their CSR programmes effectively, the future of the whole CSR movement could come into question.

If you can’t answer the question, “what difference is your CSR programme making on the ground?” it’s hard to justify sustained investment in those programmes. It’s a question of interest to all stakeholders – to corporate executives and shareholders interested in measurable returns on investments made; to CSR programme directors, interested in enhancing and optimising on future efforts; and of course to consumers, activists, and workers interested in the actual improvement of standards in the factories.



Dr Donna E Chung is trade and labour compliance advisor at Sandler, Travis and Rosenberg, based in Washington DC.





CHILD LABOUR IN COTTON'S SUPPLY CHAIN

Ethical sourcing goes beyond factory audits and supplier compliance codes, right back to where the raw materials come from and how they are produced. As cotton is a component part of many big brands' supply chains, the revelations about labour abuses in major cotton exporter Uzbekistan, including forced child labour, are becoming a major concern, and one that buyers cannot ignore.

The central Asian republic of Uzbekistan is the third largest exporter of cotton in the world. Weighing at around 800,000 tonnes a year, Uzbek cotton exports are worth \$1 billion, and generate "around 60% of hard currency earnings" for the country, according to the London-based non-governmental organisation Environmental Justice Foundation.

According to EJF, human rights violations are endemic in Uzbekistan's cotton production. Most disturbingly, thousands of school children are removed from classes during the harvest season to supplement the agricultural workforce. Government officials close schools for up to three months and transport the students and their teachers to camps in the cotton-growing regions. Working for minimal wages, young children spend long days in the fields manually picking cotton. Required daily quotas are high, and failure to meet

them is punished by scoldings or even beatings. And while child labour can be commonplace in many countries, the situation in Uzbekistan is unusual in that it is the authorities that are forcing children into the fields and not a case of them helping out on their family farm.

The International Labor Rights Forum says that in total "up to one-third of the country's workforce labours on cotton farms" and that "independent union representation is almost nonexistent for workers".

Patricia Jurewicz is associate director of the corporate responsibility programme at As You Sow, a shareholder advocacy organisation. She says that a lot of the problems in Uzbekistan stem from the fact that "the government controls the entire production process throughout the cotton supply

chain". And it is Uzbek president Islam Karimov and the country's controlling elite that directly benefit from profits the industry generates, while the vast majority of the three million Uzbek farmers and agricultural workers live in conditions of extreme poverty. As EJF comments: "Thousands of children are ordered to pick a crop that benefits the government, not their families."

Jurewicz offers some clues as to why the forced and child labour issues that have emerged regarding Uzbek cotton have slipped through the net, in terms of buyer awareness, for so long. "Many companies were a bit overwhelmed dealing with issues in factories. Attention and resources were focused there, which meant that other supply chain matters got ignored. Plus, when brands feel far removed from the problem, they do not feel it is their responsibility to police something that may or may not be in their product."

Raw materials sourcing issues are not unique to cotton, though. Jurewicz highlights earlier revelations regarding child labour in the African cocoa industry and, in 2006, the production of Brazilian pig iron that similarly has affected the US auto industry. But the focus has shifted to the cotton supply chain, particularly following the broadcasting of a BBC news story in October 2007. The socially-responsible investment community has a role to play in such circumstances, Jurewicz believes. There are strict rules regarding "no child or forced labour in supply chains" before SRI funds can consider investing in a company, and "although the companies in the current SRI portfolios may not be using forced or child labour themselves, it is unacceptable in any part of their supply chains," Jurewicz adds.

Europe has been the main market for Uzbekistan's cotton, and now some big European brands are stating publicly that they will not source from the country. Jurewicz points out that as a cotton-exporting nation itself, there is not a great deal of raw Uzbek cotton coming into the US. "However, we are importing tonnes of finished apparel from China, Russia, Bangladesh and India. Where are they getting their fabric? And there is cotton in more than just the base material – think about zippers, thread and other cotton trims," she says. "Buyers need to ask the tough questions of their suppliers. Where are they sourcing their cotton from? Could any of it be coming from Uzbekistan?"

Campaigners agree that there are potentially serious risks for brands that do not investigate where the cotton in their supply chain is coming from. Jurewicz highlights that the

US State Department is convening concerned government agencies and an array of US stakeholders to provide a forum for different parties to communicate their concerns and potential actions to take regarding the Uzbek cotton issue. "This is an area where national authorities need to take the lead and co-ordinate with international institutions and their constituencies, and urge the Uzbek government to stop denying the problem," she says.

WHAT BUYERS CAN DO NOW

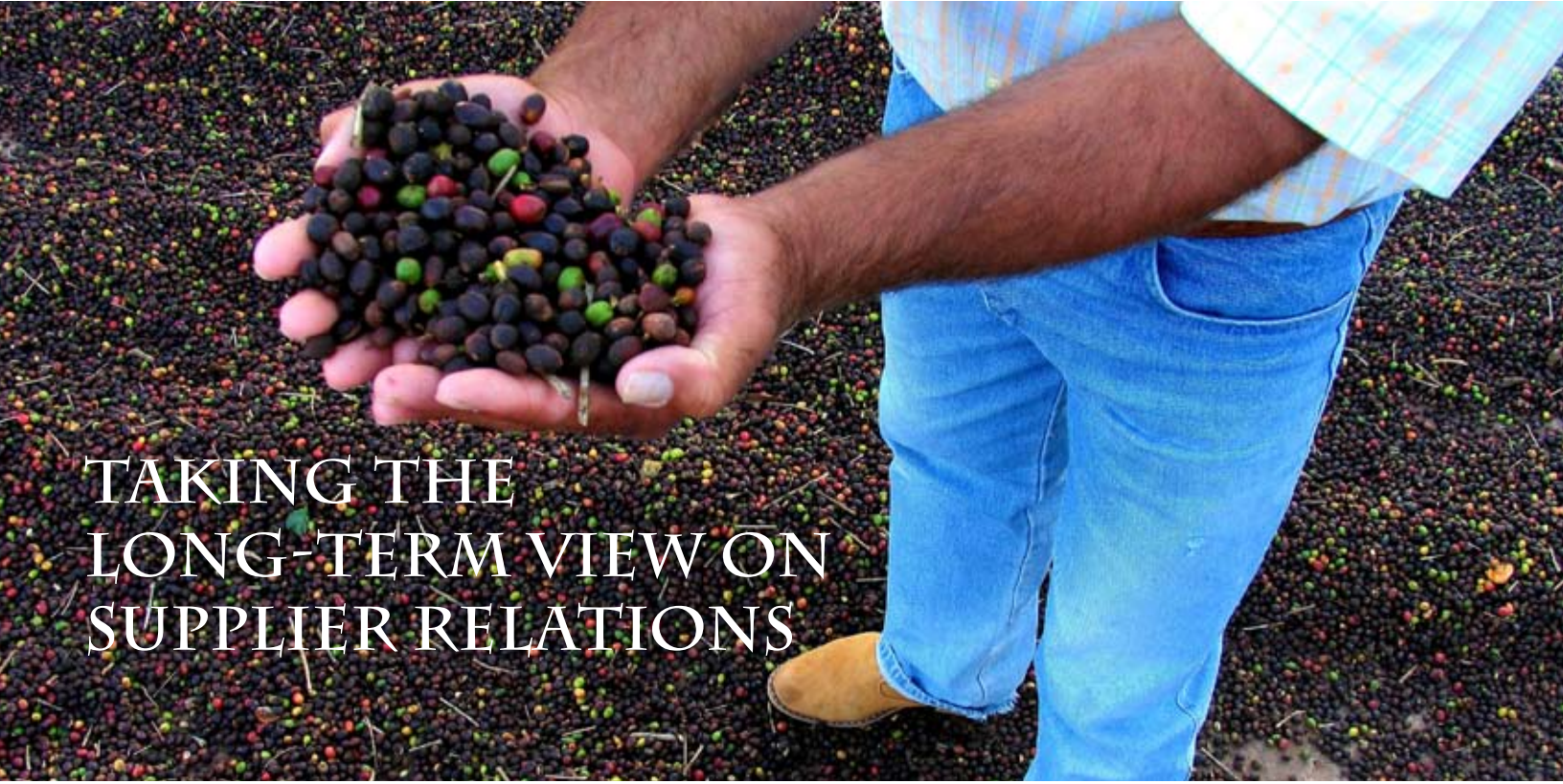
The Environmental Justice Foundation has some recommendations for brands or buyers concerned about Uzbek cotton in their supply chain.

- Work with civil society organisations to develop an effective product labelling system, guaranteeing that neither child nor forced labour is used at any stage of the production process.
- Take immediate steps to make available to customers information on the origins of all cotton products (not only the country of manufacture of the item).
- Undertake an independent review of cotton suppliers – including Uzbek government-owned trading companies – and seek assurances that the cotton is produced in accordance with international labour norms. Where assurances cannot be provided, alternative suppliers should immediately be sought.
- Undertake commitments to be more transparent in the agreeing of contracts with Uzbek government agencies.
- Avoid procurement of Uzbek cotton until such time that child and forced labour are eradicated from the production process.
- Engage with civil society groups and international organisations in joint efforts to improve working conditions on cotton farms and remuneration provided to farmers and other workers.

Source: "White gold: the true cost of cotton", Environmental Justice Foundation

A DEAD SEA – COTTON'S LEGACY

Bordering Uzbekistan to the north, the Aral Sea was once the world's fourth-largest body of water, some 68,000 square kilometres in area. But since the 1960s it has shrunk to around 10% of its original size, now comprising a series of partially interconnected highly saline lakes. A major culprit has been the diverting of rivers and watercourses to irrigate thirsty cotton crops in Uzbekistan, a process initiated under Soviet rule 50 years ago, and accelerated in recent decades. Many of Uzbekistan's canals and man-made irrigation channels are of poor construction, allowing chronic leakage and evaporation so that only a small fraction of the water diverted from the Aral's supply actually reaches the cotton fields.



TAKING THE LONG-TERM VIEW ON SUPPLIER RELATIONS

Insisting that suppliers abide by a fixed set of social and environmental standards is one thing, but how should buyers relate to suppliers in practice? Starbucks is an example of a company that has developed an innovative social responsibility programme that integrates ethics into its supply chain.



Some companies with a real interest in corporate social responsibility set up dedicated departments to promote higher standards among their suppliers. While Starbucks does have some employees who focus on improving social and environmental standards throughout its supply chain, **Virginia Bergin**, Starbucks regional manager for sustainable procurement practices, says that the company tries to ensure that the entire staff is aware of CSR policy. She says: "The supplier social responsibility programme is integrated in the whole corporation. It's a shared initiative throughout the entire organisation."

Starbucks has a series of CSR standards on which it takes a zero-tolerance stance: all suppliers must comply with them.

For instance, the factory must be transparent and show real wage and hour records. If not, Starbucks will cancel all production orders. For other aspects of its social responsibility programme, the company is prepared to work with suppliers that fail to comply but which are prepared to demonstrate a concrete commitment to meeting these goals over time. For instance, where employees work a 75-hour week, this must be gradually reduced to a maximum 60-hour level according to an agreed schedule.

The company tries to help suppliers to identify problems and then find their own solutions. "When deciding how to implement our programme in a particular factory, we look at country risk and at how effectively particular countries implement their own labour laws," Bergin says.

“It helps if suppliers hear it from the buyers directly. We train the buyers on sustainable procurement internally and build monitoring into their training programme. Then through our assessment process we focus on continuous improvement. In China, for instance, we bring buyers and suppliers together on a quarterly basis. We explain that the supplier social responsibility programme is part of our wider CSR.”

Getting boardroom agreement at suppliers is crucial. Bergin says: “Senior management in the supplier factories need to be on board from the start and communicate the CSR requirements down through the firm. Everyone needs to understand the implications.”

“Senior management in supplier factories need to be on board from the start”

Virginia Bergin

Whether or not working with suppliers that employ poor labour standards is the best method of ensuring social responsibility within Starbucks’ supply chain remains to be seen. But, Bergin says: “The ‘comply or die’ policies of the past created problems with transparency, so Starbucks aims to bring about real change through our current programme. We try to engage on labour and human rights by demonstrating the business case for CSR. We seek to demonstrate that good management systems are more efficient.”

Stronger relationships

Bringing suppliers into the CSR process has paid dividends for both sides, as Starbucks is able to build stronger long-term relationships with factories that know that the company supports their changes. Bergin says: “Long-term relationships are vital. It’s very hard to conduct assessments and effect change in the short term.”

Starbucks uses third-party monitoring organisations to assess how well suppliers are abiding by the agreements that have been reached. Its main monitoring partner is Intertek, although it also works with Level Works in China. In addition, Starbucks works in the field itself, shadowing its third-party monitors. “Our third-party monitors use a combination of local and international laws – as well as our own standards for manufactured goods and services – but where there is a conflict between them they go with the highest standard,” Bergin says.

Other companies also monitor many of Starbucks’ supplier factories. This raises the issue of audit and code fatigue, where suppliers are presented with a different set of standards based on different approaches by each international customer with a social responsibility programme. Co-operation between purchasing companies is frequently the best policy – and to harmonise standards where possible is a goal – so Starbucks now works with other brands at the factory level in some countries. The collaboration is limited, however, due to confidentiality agreements with the factories. The company hopes to increase factory-level collaboration opportunities in the future through its participation in the Fair Factories Clearinghouse.

The integration challenge

Integrating the traditional demands of price, quality and timing with the new requirements of CSR is always a challenge and one that Starbucks’ lack of a formal scorecard could make more difficult, although the company is considering developing such a scorecard in the future. Buyers are closely involved in the implementation of the programme, and factory performance for CSR is a deciding factor in awarding business, though there isn’t a formal tool to support this.

Yet the role of long-term relationships with suppliers is what matters for Starbucks. And the long-term results of the company’s strategy of constructive engagement should provide further evidence of the value of this approach.



THE BUSINESS CASE FOR CSR

Starbucks defines CSR as conducting business in ways that produce social, environmental and economic benefits for the communities in which it operates and for the company's stakeholders, including shareholders. A few of the benefits are:

- Attracting and retaining partners: Starbucks believes that its commitment to CSR leads to higher than typical levels of satisfaction and engagement among its partners.
- Customer loyalty: studies have revealed that customers prefer to do business with a company they believe to be socially responsible, when their other key buying criteria are met. It believes customer loyalty has been a driving force behind its growth and success.
- Reducing operating costs: many environmental measures, such as employing energy-efficient equipment or lighting, involve initial investments but deliver long-term environmental and cost-saving benefits.
- Strengthening the supply chain: to have a sustainable business requires a reliable and responsible supplier base that can keep pace with growth. Starbucks invests in measures to help its suppliers to do so.
- Licence to operate: having a strong reputation as a socially responsible company makes it more likely that there will be a welcome in a local community.

GOOD PRACTICES PAY OFF

Starbucks has developed its Performance Improvement Planning programme in conjunction with Intertek to inspire a culture of continuous improvement among suppliers.

Virginia Bergin highlights one example of how this programme has worked successfully in practice. Starbucks identified a Chinese factory as a potential supplier. The initial assessment revealed that the company met the zero-tolerance standards but problems emerged later in several areas, particularly on wages and health and safety standards. In particular, overtime was commonplace and the company suffered from staff turnover of 30% a year.

Starbucks tried to give the factory incentives to address its overtime problems while the factory owners identified a number of positive changes that could help to improve the situation. The factory agreed to improve the lines of communication between managers and workers, partly through the creation of a workers' committee, while free meals and recreational facilities were provided for workers. Now staff turnover is down while quality, wages and efficiency have all increased.





**CASE STUDIES:
LEVI STRAUSS AND HP
CO-OPERATING WITH
COMPETITORS AND
ENGAGING WITH SUPPLIERS**

While the argument over whether or not to audit factories and suppliers is perhaps being won, the next challenges are to find the best ways of using audit data and, increasingly, exploring ways in which this data can be shared with other brands for mutual benefit.

Speaking to *Ethical Sourcing Report*, **Leslie Croshaw** from Levi Strauss explains the background to the company's ethical sourcing policies and also why it has taken steps to work with competitor brands in shared factories. And HP's **Bonnie Nixon Gardiner** outlines how electronics' biggest player works with its supply chain, why the industry co-operates within the EICC, and argues the case for making supplier lists public.

Levi Strauss – dealing with audit fatigue

Leading clothing brand Levi Strauss is committed to working at the “factory, community and public policy levels to ensure that the people making [its] products are treated with dignity and respect, and work in safe and healthy conditions”, according to the Corporate Citizenship section of the company's 2007 annual report.

The company believes that by working with other brands in shared factories, it is possible for working conditions to

be improved while concurrently reducing the burden on suppliers with fewer factory audits and visits. Levi's took the first step in this direction in 2005 when it revealed its supplier list, while suggesting to other brands that it was time to investigate how to co-operate, to the benefit of all parties.

Leslie Croshaw, manager for supply chain social and environmental sustainability at Levi Strauss, says that while it took some time and energy for the company to get to this stage, there was a commitment to see the process through.

"It wasn't just about developing the transparency that NGOs had been asking for – we saw the opportunities for co-operation with our competitors that would be for the benefit of everybody."

Initially, Levi's wrote to a number of competitor brands suggesting there were grounds for co-operation in shared factories. At first it was a question of "if we do share information, what would we share?" Croshaw says. "Different brands were able to provide different levels of information."

"We saw the opportunities for co-operation with our competitors that would be for the benefit of everybody"

Leslie Croshaw

And, of course, US anti-trust rules have been foremost in many minds, with company legal teams all very careful to keep co-operation within the proper parameters. Croshaw explains: "As a general guide, we can speak with other brands about conditions in the factory, but not about orders or volumes."

In 2008, Levi's is now working with 15 other brands across 135 factories, sharing the results of monitoring exercises and formal audits, and co-ordinating on remediation plans and training for capacity building. The co-operation means that Levi's, along with the other brands involved in the programme, has significantly more information available on many of the suppliers from which they source. Levi's says that it has been able to reduce the number of audits in factories shared with other brands by about 25%.

The factories significantly benefit from this brand co-operation programme. "A typical factory might be receiving up to 25 visits annually from brands or third-party monitors, but if two or three of these brands can co-operate then up to nine visits might no longer be required," Croshaw says. This means, of course, that rather than showing more and more inspectors round the facilities, factory management can actually get on and deal with the issues that audits identify as requiring attention. And, from the worker welfare perspective, "if there are two factory customers asking for improvements to be made, that carries more weight than if it was just one."

The information-sharing process has been something welcomed by Levi's staff in the field. "They've found it an

empowering experience," Croshaw says. Of course, field staff can be in the best position to be able to make suggestions about problems at local factories and indicate possible remediation measures. "They can now actively look for creative ways to solve the problems – and are encouraged to do so." Clearly, local staff working for different, competing, brands are bound to be aware of one another, and in many cases are likely to be well acquainted. Information sharing means that they can, in some areas, carefully work together for mutual success.

But just to get CSR initiatives on the senior management agenda at major multinational corporations, let alone making it a priority, is a task many supply chain or sourcing teams find themselves facing. Croshaw says that it is important to find a champion among the senior team who "gets" what corporate responsibility and ethical sourcing is really all about. "That's what happened at Levi Strauss," she says. "Not everyone buys into the agenda, but we had senior management, right at the top, who were on board."

Looking to the future, Croshaw sees scope for continuing to look for commonalities in audits and audit procedures, and she thinks that pushing for ever-increasing transparency is what will keep driving the process forwards.

For more information see www.levistrauss.com/Citizenship

HP – partnering with suppliers

Promoting more supply chain transparency was very much part of the process for IT giant HP when it announced its list of suppliers. **Bonnie Nixon Gardiner**, HP's global programme manager for its supply chain social and environmental responsibility programme, says: "We wanted to say 'we are proud you are our partner' but more importantly 'now we are public about it.'" This means that HP's ethical supply chain policies are up for scrutiny and that there can be "no excuses" from the company and its suppliers alike.

HP sees its relationship with suppliers very much as a partnership. Nixon Gardiner says: "It's not just about policing. There is a great deal of mutual respect. But in the same way as we work with suppliers on design and quality, we work with them on social responsibility." She is proud of HP's investment in strategic mentoring in the company's supply chain. "If there is a problem we ask 'why are you not getting it right?' and 'what can we do to help?'"

Nixon Gardiner is also pleased to be involved in the Electronic Industry Code of Conduct (EICC – see box on p22). “Taking an industry approach, where we can all learn from others, is very important,” she says. “There is no point in repeating work just for the sake of it if there is information that can be shared. EICC is making great progress, and it’s an initiative that HP has been involved in from the start.”

When dealing with supply chain issues, Nixon Gardiner says that it’s important not to get lost in the minutiae, but stay clear that auditing and remediation programmes should be about the workers and factory conditions. “Focus on worker ownership – while we can enable the process, they have to own it,” she says. Creating an environment where this is possible is a large part of the battle.

“Focus on worker ownership – while we can enable the process, they have to own it” Bonnie Nixon Gardiner

Leading on from this approach, Nixon Gardiner stresses the need to deal with the root causes of problems, and developing an understanding of them. She highlights the problems that can occur where there is a rapidly expanding economy and large numbers of factories being established in short time periods. “In Chinese cities, for example, there might be eight million migrant workers, but a civil infrastructure for less than two million.” Workers might then not have access to healthcare, legal or financial services – not because they are actively being denied them, but simply because there is no capacity for them. That is, of course, unless their employer provides them – and it is not uncommon for governments to say that it is the responsibility of the company to do so. Understandably, “this situation is something that people in developed nations sometimes struggle to understand,” Nixon Gardiner says.

A key part of drilling down to the root causes of the issues is to take care not just to treat the symptoms of a problem. Nixon Gardiner says: “In some respects a ‘tick-box’ mentality on its own doesn’t solve anything. Yes, audits are a vital tool, and we have to have a presence in the factories, but what’s important is an understanding of what’s behind management systems.” She argues that establishing a series of key performance indicators is “a sustainable fix and a way to really solve problems”.

And often the best solutions come from the factory management and the workers themselves. “Involve them in the process,” Nixon Gardiner suggests. “Sometimes they might not even realise that they have the answers.” In other words, it’s about empowerment.

HP is involved in a HERproject (Health Enables Returns) programme at two of its supplier sites in Mexico and at several in China. “Many IT manufacturing workers are female. It’s an attractive workplace environment for them as there’s no heavy lifting and it’s relatively clean and secure. This means that a lot of the health issues affecting a workforce are consistent.” The HERproject provides advice about health issues and also other relevant matters, including domestic violence and education. “I think this sort of peer education model can really work – and could even be extended to other areas,” Nixon Gardiner argues.

The bottom line, though, is to keep focusing on the business case that, for suppliers, it is good for the company’s prospects to treat employees properly. “It’s not rocket science – it’s just common sense,” Nixon Gardiner says. A content workforce is a productive one. Enticing employees to stay keeps turnover costs down. And now that HP has made public its supplier list, there is a further motivation for its suppliers to improve worker conditions. “Factories are proud to be on our list. But now they have to be more accountable.”

For more information see:

www.hp.com/hpinfo/globalcitizenship/environment/supplychain/index.html

www.hp.com/hpinfo/globalcitizenship/gcreport/supplychain.html



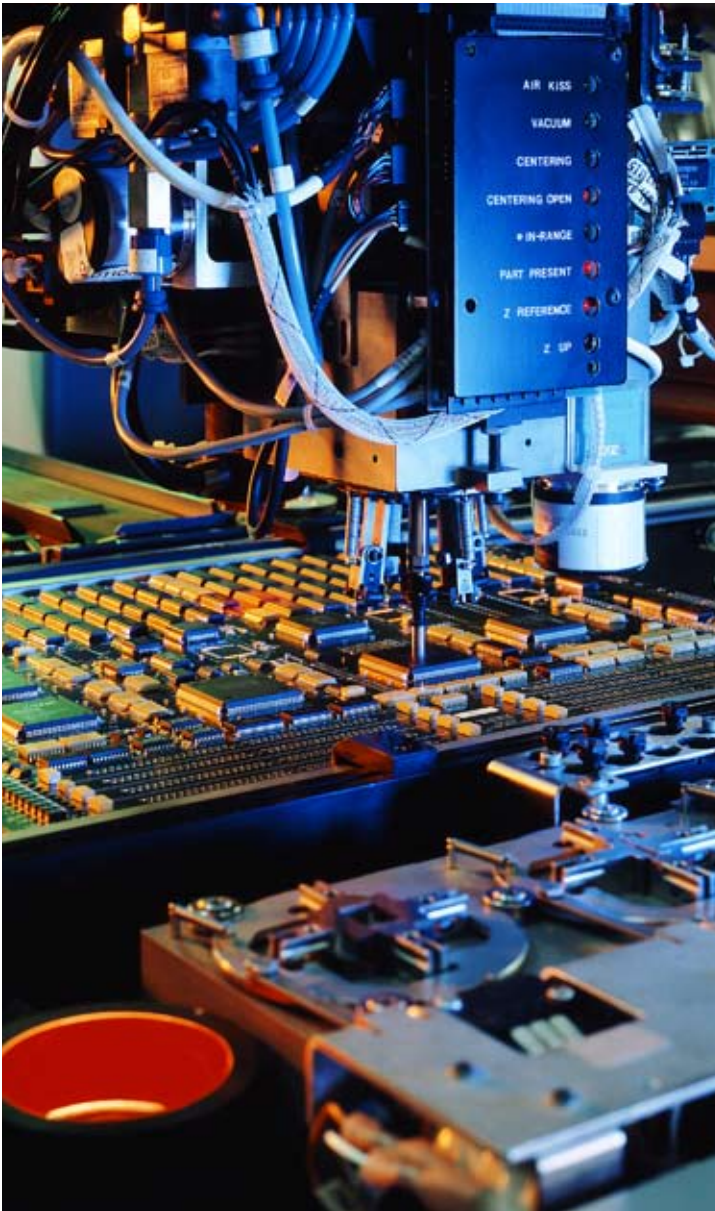
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ELECTRONIC INDUSTRY CODE OF CONDUCT – THE WHAT, WHY AND HOW

The Electronic Industry Code of Conduct outlines standards to ensure that working conditions in the electronics industry supply chain are safe, that workers are treated with respect and dignity, and that manufacturing processes are environmentally responsible.

To adopt the code, a business shall declare its support for the code and seek to conform to the code and its standards in accordance with a management system as set out in the code. Participants should regard the code as a total supply chain initiative. At a minimum, participants shall require its next tier suppliers to acknowledge and implement the code.

Fundamental to adopting the code is the understanding that a business, in all of its activities, must operate in full compliance with the laws, rules and regulations of the countries in which it operates. The code encourages participants to go beyond legal compliance, drawing upon internationally recognised standards, in order to advance social and environmental responsibility.

The code is made up of five sections that outline standards for: labour; health and safety; the environment; the elements of an acceptable system to manage conformity to the code; and, business ethics.

EICC was initially developed by a number of companies engaged in the manufacture of electronics products between June and October 2004, which included Celestica, Dell, Flextronics, HP, IBM, Jabil, Sanmina SCI and Solectron.

Source: Taken from the EICC Code of Conduct. For more information go to www.eicc.info



PUTTING GOOD GREEN INTENTIONS INTO PRACTICE

Corporate social and environmental responsibility is a growing concern for supply chains. Products are increasingly being branded as “green” or “derived from environmentally sustainable sources”, but how can the image and the greenwash be separated from genuinely sustainable procurement strategies? **Lorraine Smith** from Canadian Business for Social Responsibility (CBSR) has some answers.



“Many companies now openly express their commitment to social responsibility, but the level of their activities varies a lot. Consumer-facing companies are certainly becoming more concerned, and this is being noticed and discussed in the mainstream more than

the activities in other sectors such as mining or forestry in spite of a long history of social responsibility in these other sectors,” says CBSR’s **Lorraine Smith**. The brands making a real difference are working hard behind the scenes in ways that the general public often fails to detect. The challenge for socially and environmentally responsible companies is to use their sustainable procurement strategies to support their CSR and environmentally aware image.

Companies are becoming increasingly aware of their environmental image, in large part because of growing concern over

climate change. Smith says: “Four years ago at the Intertek conference, factory compliance was the big thing. Delegates were clearly focusing on human rights and labour law. At this year’s conference, social and environmental factors seemed to carry equal weight in discussion of sustainable procurement strategies.”

“We’re in the infancy of understanding the environmental and social impact of our decisions”

Lorraine Smith

She agrees that there has been a big growth in companies outside the retail sector that are also interested in sustainable procurement. “The first place they tend to look is paper:

where do they source their paper, how is it produced and how much of it do they waste? But further implementation, for example office furniture or computers, is often much more difficult.”

Green queries

The drive to associate products with environmental interests has resulted in a wave of greenwash, where products are positioned differently, perhaps through a packaging revamp, but no substantive changes have been made in the procurement chain. Smith says: “Not all the current interest in the environment is greenwashing, but there is often a lack of vigour and sophistication behind the claims, even if they are made for genuine reasons.

“There is a lack of information and knowledge surrounding the subject, which is understandable to an extent. We’re in the infancy of understanding the environmental and the social impact of our decisions.”

But perhaps the widespread evidence of greenwashing at least means that companies are starting to think about the social and environmental impact of their operations? Not so, Smith says. “I don’t see anything good in greenwashing. We must encourage companies to be able to back up statements.”

Greenwashing is enabled by the lack of legal or regulatory checks on companies’ claims, as phrases such as “CSR”, “carbon neutral” and “carbon offset” mean different things to different people. It is therefore easy to make claims that have little substance. As a result, surveys repeatedly demonstrate that consumers believe companies can have a huge influence on climate change and on working conditions through their supply chains; yet at the same time consumers largely consider corporate social responsibility and environmental policies to be greenwash.

Now, innovative trade associations and cross-business organisations, including CBR, are making it their mission to improve environmental and social performance. While non-compliance with overtime regulations remains a big worry, it is difficult to separate the social and environmental effects of many problems. For instance, air quality affects workers as well as the environment beyond the factory, as does waste disposal.

One of the biggest concerns in international procurement in recent years has been the discovery of lead in the paint used

on toys. Not only does this affect the health of the workers on the production line as well as the children who play with the toys, but it also has implications for landfill. Ethical trade demands that companies demonstrate that they are aware of the implications of their supply chain and then implement effective codes of conduct. This is equally valid with both social and environmental implications.

The solution

Smith says that how we get from the current environment of great interest and limited action depends on whether each company can identify key goals. No single firm can put as much effort into mitigating all the negative social and environmental effects of its procurement, while accentuating the potential positive effects. “Each company has to identify where it can make the most impact. If it’s a brand that is CSR-aware and climate change is of concern to its customers, then it needs to identify its biggest sources of greenhouse gas emissions and that is not always where you expect it to be.”

“Downward pressure on price has led to a lot of social and environmental damage”

Lorraine Smith

The biggest hurdle is not “do they really mean it?” but “how do you do it?” Smith believes. She argues that the issue of greenwash is in its infancy not because companies and consumers don’t care and just want a superficial answer, but because we are generally still unsure of the questions to ask and the best answers to expect.

CBR considers that the balanced scorecard approach is the best option for companies seeking to turn image into reality. Instead of just focusing on price, quality and timing in their procurement strategies, they now also need to include environmental and social considerations if they are to turn CSR policies into more than just a set of goals. Smith advises: “Let stakeholders know if you make the right choices: reputational payback will serve you well.”

In its Good Company Guidelines, CBR lays out a series of checklists that companies can use in their relations with suppliers, consumers and other stakeholders. In each case, the organisation recommends a staged approach to implementation. Once a commitment has been made, a firm policy must be drawn up, a programme designed that is subject



to evaluation and management, with stakeholders involved. Importantly, the whole process must be transparent and accountable.

Certainly, putting good intentions into practice is not always easy. Smith gives an example of a large retail firm that is expanding by opening new branches across Canada. It wants to make a positive impact on every community where it operates but recognises that building new stores on greenfield sites, where land is cheaper, can have a negative environ-

mental impact. It is currently assessing how to marry its business model with its policy on corporate social responsibility and is meeting with key stakeholder groups to discuss how to achieve this.

Consumers too

Consumers also have a role to play. To take the example of packaged retail products, consumers need to ask themselves whether all ingredients are disclosed; whether they contain recycled content; and whether the packaging is designed to minimise waste and maximise shipping. They also need to consider whether the product is designed for long-term use and whether it contains known carcinogens, hormone disruptors or other hazardous substances. In addition, the post-consumer result of the product is not always obvious, as many biodegradable products may end up in landfill where they cannot biodegrade in the short term.

Smith agrees that change will take a long time but believes that consumer pressure is not enough because consumers are not critical or well informed enough. "Downward pressure on price is what has led to a lot of social and environmental damage. We can do things better but it will cost more and now may be a difficult time to effect change because of the global economic downturn." She

says that capital markets need to be steered towards environmentally and socially aware investment, but it is clear that promoting sustainable procurement will not be achieved overnight.

**What is greenwash?
How to make sure your supply chain is green**

<p>APPLY THE STAKEHOLDER APPROACH</p>	<p>Without stakeholder input and analysis, the greening of operations and products risks:</p> <ul style="list-style-type: none"> • Only solving a small part of the problem; • Creating unintended consequences; • Alienating those who it's meant to benefit; and • Missing key opportunities.
<p>TAKE THE GREENWASH TEST</p>	<p>There may be a greenwash situation if:</p> <ul style="list-style-type: none"> • Nothing has changed except the positioning or messaging of the product; • One issue is picked and focused in a positive way and all others are ignored; and • Unsubstantiated claims are made.
<p>THE LIFE-CYCLE APPROACH</p>	<p>Use life-cycle analysis (LCA) to identify and prioritise which impacts can be affected:</p> <ul style="list-style-type: none"> • Raw materials; • Manufacturing (all stages); • Distribution; • Consumption; and • Disposal.
<p>SETTING GREEN GOALS</p>	<p>Ask questions to develop your goals:</p> <ul style="list-style-type: none"> • What impact do we want to have on stakeholders, the environment and our business? • How will we measure this impact? • Has the full life-cycle analysis been included? And if not, why? <p>Follow up:</p> <ul style="list-style-type: none"> • Measure the impact and adapt the strategy; and • Review results with stakeholders.

Source: Lorraine Smith, CBSR

Note: Lorraine Smith is an independent consultant, and until recently senior CSR adviser at CBSR. Smith remains an associate consultant for CBSR.

SUPPLIER CHECKLIST

1. Incorporate social and environmental values into purchasing decisions.
2. Make fair and prompt payment.
3. Prioritise local suppliers.
4. Ensure all qualified businesses have the opportunity to supply.
5. Do not enter into business relationships with companies that use compulsory labour.
6. Inform suppliers of the company's procurement standards.
7. Ensure directors and senior managers practise supply chain risk management.
8. Gather and promptly respond to supplier complaints.
9. Involve suppliers in supplier contract development: (a) performance indicator development; and (b) contract evaluation.

Source: CBSR

COMMUNITY CHECKLIST

1. Make explicit community commitments:
 - (a) business basics: meet community demands for cost effective products and services;
 - (b) philanthropy: meet community needs without apparent business benefit;
 - (c) commercial initiatives: partner community-based organisations that support business success; and
 - (d) community investment: engage in long-term strategic community partnerships.
2. Donate 1% of pre-tax profits.
3. Prioritise local employment and suppliers.
4. Incorporate social values into purchasing decisions.
5. Consider local/regional employment and training needs in human resources strategy.
6. Have a board and management team that understands community interests.
7. Conduct social and environmental impact assessments.
8. Gather and promptly respond to community complaints.
9. Involve community stakeholders in:
 - (a) programme definition;
 - (b) performance indicator development; and
 - (c) programme evaluation.

Source: CBSR

CHINA'S DEVELOPING ENVIRONMENT LAWS



With Chinese factories a feature of many supply chains, brands need to keep up with China's statutory environmental requirements. In an interview for Ethical Sourcing Report, **Shen Xiaoyue**, from the Policy Research Centre for Environment and Economy of the State Environmental Protection Administration, explains the basis of China's environmental laws, how they are applied, and some key issues of which companies operating in the country need to be aware.

Q: How have China's environmental laws developed over the past few years?

A: China's environmental protection law system has gradually been established with the development of environmental protection measures, which have become the basis of China's environmental protection efforts. The legal environmental protection system is integrated and independent, consisting of associated and co-ordinating laws, regulations, rules, standards and international treaties on environmental protection. It is based on the Constitution of the People's Republic of China, with the basic law of environmental protection at its core and provisions on environmental protection in other related branches of the law supplementary to this.

So far, China has formulated nine environmental protection laws and 15 natural resource laws. China has introduced:

- Over 50 administrative regulations on environmental protection;
- Nearly 200 department rules and regulatory documents;
- 17 military environmental protection laws and regulations; and
- Over 800 national environment standards.

And, the government has approved and signed more than 50 international environmental treaties.

Local People's Congresses and local governments have established more than 1600 local environmental regulations.

A legal environmental protection system has been initially established that reflects China's actual situation.

Environment protection legislation is one of the most active and fastest-growing fields in the legal system. In less than 30 years, China has established a relatively integrated legal system, developed from nothing.

Q: What has been the time-frame for these developments?

A: After the United Nations Conference on Environment and Development in 1992, China's environmental legislation entered a new stage of development guided by the concept of sustainable development.

The Chinese government formulated 10 Strategies on China's Environment and Development and issued China's Agenda 21 – White-Book of China 21st Century on Population, Environment and Development. Over a period of more than 20 years, significant breakthroughs have been achieved in China's environmental protection standards, environmental legislation technologies and a number of laws.

During this period, China has revised some outdated laws and regulations and continuously improved and refined the environmental law system.

- Solid waste pollution: People's Republic of China Law on the Prevention and Control of Environmental Pollution by Solid Wastes was formulated in 1995 and revised in 2004.
- Atmospheric pollution: People's Republic of China Law on the Prevention and Control of Atmospheric Pollution formulated in 1987 was amended in 1995 and in 2004.
- Noise pollution: People's Republic of China Law on the Prevention and Control of Noise Pollution was formulated and implemented in 1996.
- Marine environment protection: Marine Environment Protection Law of the People's Republic of China was amended in 1999.
- People's Republic of China Law on Promoting Clean Production and People's Republic of China Law on Assessment of Environment Impacts were formulated in 2002.
- People's Republic of China Law on Prevention and Control of Radioactive Pollution was formulated in 2003.
- People's Republic of China Law on Prevention and Control of Water Pollution was amended in 2008 and will go into

effect on June 1st 2008.

In addition, amendments of other basic laws have improved the regulation of environmental protection. In 2007, Crime of Violating the Protection of Environment and Resources was included in the Criminal Law in the form of a special chapter, which was a major breakthrough in Chinese legislation. The Supreme Court promulgated The Interpretation on Some Issues Concerning the Specific Application of Law in the Trial of Criminal Cases Involving Environmental Pollution which details standards for conviction and sentencing as specified in the People's Republic of China Criminal Law. It makes the investigation of environmental criminal responsibility more practical.

In November 2001, China joined WTO, an indication that China's economic development is geared to international standards. Furthermore, China has entered the International Convention, which accelerates the development of environmental legislation.

Q: What have been the significant milestones during the process of development?

A: Since the United Nations Conference on Environment and Development, China has been determined to change unsustainable production and consumption methods and proceed on the basis of a sustainable development strategy. The formulation of China's Agenda 21 was for this purpose.

Sustainable development has brought comprehensive and far-reaching effects on China's environmental law construction. There is now an increased emphasis on prevention principles, entire process management, clean production, sourcing control and totality control in the environmental law system.

With the penetration of the sustainable development strategy and integrated environmental management, the scope involved in China's system of environmental law has grown from an initial control of individual elements (such as the "end control" of pollution with an emphasis on pollutant treatment and disposal) to the entire process control including the decision-making process (such as "pollution source control" and entire process control "from beginning to end"). From, initially, management of individual issues or certain types of issues (such as waste management), now the focus is on the management of varied related matters (such

as waste management and product management, resource management and environmental management).

In addition, some new legal systems are now being promoted in China, such as integrated decision-making systems, comprehensive assessment for environmental impacts, environmental labelling systems, clean production systems, new environment and resource tax systems, and discharge permit systems.

Q: What is the break-down of responsibility for environmental issues at a national and regional level?

A: According to the People's Republic of China Law on Environmental Protection, the administrative department of environmental protection directly under the State Council shall implement unified supervision and administration of environmental protection all around China. The administrative departments of environmental protection under local governments above county level shall implement unified supervision and administration of environmental protection in local areas.

The administrative department of environmental protection directly under the State Council shall establish state pollutant discharge standards according to environmental quality standards and the economic and technological conditions of the state.

The people's government of any province, autonomous region or municipality may, for issues not provided in the state pollutant discharge standards, work out local standards. For issues covered by the state standards for pollutant discharge, local authorities may also devise local standards that are stricter than the state standards. Such standards should be filed with the administrative department of environmental protection under the State Council. Companies that discharge pollutants in areas where the local standards for pollutant discharge have been established shall observe such local standards.

Q: For companies currently operating in China or wishing to set up operations in China, what are the key requirements of China's environmental laws?

A: According to the People's Republic of China Law

on Environmental Protection, companies that cause environmental pollution and other public hazards shall incorporate environmental protection into their plans and establish a responsibility system for environmental protection. They must adopt effective measures to prevent and control pollution and harm caused to the environment by waste gas, waste water, waste residues, dust, malodorous gases, radioactive substances, noise, vibration and electromagnetic radiation generated in the course of production, construction or other activities.

"If an enterprise or institution has caused severe environmental pollution, it shall be required to eliminate and control the pollution within a prescribed period of time"

Shen Xiaoyue

Facilities for the prevention and control of pollution in a construction project must be designed, built and put into use together with the principal part of the project. No permission shall be given for a construction project to be commissioned or started, until its facilities for the prevention and control of pollution are examined and considered to have met the standards set down by the appropriate department of environmental protection administration that examined and approved the environmental impact statement.

Facilities for the prevention and control of pollution shall not be dismantled or left idle without authorisation. If it is really necessary to dismantle such facilities or leave them idle, prior approval shall be obtained from the appropriate department of environmental protection administration in the locality.

Enterprises and institutions discharging pollutants must report to and register with the relevant authorities in accordance with the provisions of the relevant department of environmental protection administration under the State Council.

Enterprises and institutions discharging pollutants in excess of the prescribed national or local discharge standards shall pay a fee for excessive discharge according to state provisions and shall assume responsibility for eliminating and controlling the pollution. The provisions of the Law on



Prevention and Control of Water Pollution shall be complied with where they are applicable. The income derived from the fee levied for the excessive discharge of pollutants must be used for the prevention and control of pollution and shall not be appropriated for other purposes. The specific measures thereof shall be prescribed by the State Council.

If an enterprise or institution has caused severe environmental pollution, it shall be required to eliminate and control the pollution within a prescribed period of time.

Q: What environmental issues will the Chinese authorities deal with next?

A: In the Outline of the 11th Five-Year Plan for National Economic and Social Development, it says that during the period of “11th Five-Year Plan”, the unit GDP energy consumption should be decreased by 20% and total discharge of the main pollutants should be reduced by 10%.

By 2010, energy consumption per 10,000 yuan of GDP should be reduced from 1.22 tonnes of standard coal in 2005 to less than one tonne of standard coal, a reduction of around 20%. Water consumption per unit of industrial added value should be lowered by 30%.

During the period of “11th Five-Year Plan”, the total pollutant discharge should be reduced by 10%. By 2010, the discharge of sulphur dioxide should be reduced from 25.49 million tonnes in 2005 to 22.59 million tonnes. The average sewage treatment rate of cities and towns should be no less than 70% and comprehensive utilisation of industrial solid wastes should be more than 60%.

Q: What issues do you think will be of the greatest concern over the coming years?

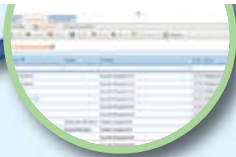
A: Firstly, establishing a solid and complete environmental law system in China; strengthening the legal responsibilities of stakeholders, especially governments’ responsibility in environmental protection; and adopting more and better economic measures in environmental protection.

Secondly, changing economic and trade growth processes; solving structural problems in environmental pollution; and solving environmental problems in the process of development, so as to promote rapid economic growth.

Thirdly, further intensifying efforts in energy saving and emission reduction, and improving environmental conditions in both watercourses and the atmosphere.



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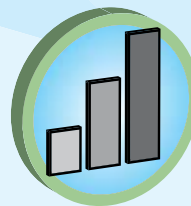
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