

Global Supply Chains: The importance of traceability and transparency

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Abstract

Around the globe, businesses are faced with increasing consumer demands to act in a responsible manner. Expectations rest not only in the hands of the corporate managers, but also throughout the supply chains of companies. Consumers who trust that a company complies with CSR standards must be able to know where and how the products they buy are made. For this to happen, a company has to track and trace its products through the entire supply chain. This essay distinguishes between different product attributes and defines two supply avenues to be traced. Furthermore, it explains the importance and benefits of transparency and traceability in supply chains and how this can be accomplished by setting and using CSR standards. Finally, the essay provides an example of a voluntary standard that was developed to improve working conditions at manufacturers and suppliers, and concludes that even state-of-the-art standards have flaws in their implementation mechanisms.

“You know so much more of a country when you haven’t seen it.”¹
Mark Twain, Sydney, Australia, 1895

Introduction

Child labour, sweatshops, global warming, deforestation: Many European governments believe that consumers will eventually reward companies that do what is in their power to solve these issues. If consumers purchased products and services exclusively from companies that comply with renowned and widely accepted CSR standards, unsustainable or irresponsible enterprises would cease to exist. However, at present, even those consumers who wish to make *a difference* are often unable to exercise critical choice because they do not have sufficient access to information on the conditions under which products are made. This issue was made clear by the European Commission in 2006: “Consumers play an important role in providing incentives for responsible production and responsible business behaviour. They are expected to exercise critical choice and encourage good products and good companies. At the moment consumers lack clear information on the social and environmental performance of goods and services, including information on the supply chain.”²

**EU communication
addresses transparency
but offers no solution**

The European Commission depicts the problem quite accurately but does not propose any solutions. The only thing the Commission plans to do, according to its *Communication on CSR*, is to “examine, in consultation with all relevant stakeholders, the need for further voluntary actions to achieve the objectives of transparency and information for consumers including on issues of public health.”³

Transparency is apparently a key element in the EU policy regarding CSR. But would more transparency actually enable consumers to “exercise critical choice and encourage good products and good companies?” Moreover, can we expect consumers to choose *good products* from *good companies*, or should governments make a pre-selection by defining through legislation what *good products* and *good companies* are?

**Can we expect
consumers to choose
good products from good
companies?**

Let us first go back to Mark Twain’s quote at the beginning of this essay. When Twain first arrived in Sydney in 1895, he announced that he intended to begin writing a book about Australia at once. “You know so much more of a country when you haven’t seen it,” he declared.

Notwithstanding his supreme sense of humour, his comment bears some truth. Travellers usually know a lot about a country before they actually visit it. They acquire knowledge by reading travel guides, books and websites, and by talking to people who have visited the country before. As soon as a traveller arrives in a country for the first time, the thin line between knowledge and experience is blurred. Very often, actual experiences leave impressions that differ significantly from the impressions we have based on our prior knowledge about a country. This is why vacations can sometimes be utterly disappointing.

Now, how is this relevant to the debate about transparency and selecting *good products* from *good companies*?

Content and process attributes: Can they be traced?

Consumers think they know about the products they buy and the companies from which they buy them. They identify or recognise products through a range of aspects that can be associated with a specific product – such as the level of technology,

design, taste, reliability or trendiness. Many of these aspects are intangible and refer to characteristics that consumers cannot discern even after consuming the products. Consumers cannot, for example, taste or otherwise distinguish between oil made from genetically engineered corn and conventional corn oil. In CSR terminology, these invisible characteristics are frequently called *credence attributes*.

Credence attributes can be divided into two categories: *content* and *process*. *Content attributes* affect the physical properties of a product, although they can be difficult for consumers to detect. For example, consumers are unable to determine the amount of isoflavones in a glass of soy milk or the amount of calcium in a glass of enriched orange juice. Process attributes do not affect final product content, but refer to characteristics of the production process. *Process attributes* include the certification of products and production processes. In general, neither consumers nor specialised testing equipment can ascertain process attributes. In some industrial sectors, systems have been developed to trace process attributes and to inform consumers about these aspects. In the food sector, for example, there are many schemes such as country-of-origin, free-range, dolphin-safe, shade-grown, earth-friendly and fair trade.

When you buy a product, especially a brand-name product, you might think you know a lot about it. Most companies do all they can to inform consumers about the positive content and process attributes related to their products. They can only inform consumers adequately if they can provide clear evidence to lend credibility to the attributes. The only way to actually verify the existence of these attributes is through a book-keeping system that establishes their creation and preservation. Therefore, products need to be traceable.

Content attributes affect physical properties; process attributes are intangible

Companies have to know where their products come from, who makes them and how the products are made. Moreover, they must be transparent about their processes and provide their stakeholders with useful and timely information. By definition, transparency is about openness and communication on issues that are regarded as important to those affected.⁴ Transparency is good for business. Managing a company in a transparent manner tends to improve the flow of information within the business and thus strengthens internal controls. Transparency also enhances market trust and credibility with key stakeholders because the perceptions of a company's stakeholders are vital to the reputation of that company. Perception is a factor of the quantity and quality of information received by the stakeholders and the extent of its validity and whether it satisfies the need of the stakeholder.⁵

Transparency enhances market trust and credibility with stakeholders

The most important argument for transparency, however, might not be the business case. Societies as a whole benefit from companies being more transparent about the way they produce and conduct their businesses. Some scholars and market analysts have called this the *Enron Factor*. The transparency agenda gained momentum with the collapse of Enron. The Enron saga exposed not only the evils of greed but also the dangers of secrecy and misreporting. Disclosure and corporate governance became buzzwords.⁶

Raising the bar through standards

One effective way for companies to communicate credence attributes is to use standards. The proliferation of standards in many industrial sectors is a result of the need for measuring and qualifying content and process attributes. Stefano Ponte

Ex ante measures to prevent non-compliance, ex post liability to punish non-compliance

classifies standards in three broad categories: mandatory, voluntary and private:

“Standards are mandatory when they are set by governments in the form of regulation. These may affect trade flows by placing technical requirements, testing, certification and labelling procedures on imported goods. Governments can rely on standard enforcement through ex post liability rules that allow punitive damages to be awarded to the buyer in case of non-compliance, or they can adopt ex ante measures – such as requiring information or banning a product not matching technical standards from being imported. In the US, ex post liability is more common, while in Europe ex ante measures are the backbone of regulation. Voluntary standards arise from a formal coordinated process in which key participants in a market or sector seek consensus. The International Standardization Organisation ISO has established over 7,000 voluntary standards. Some of these are also introduced as a response to consumer request (such as eco-labels) or as a result of NGO initiatives (such as Fair Trade labelling). Sectorial organisations can also establish voluntary standards that apply to their members. Voluntary standards are usually verified through third-party auditing. Private standards are developed and monitored internally by individual enterprises. What often distinguishes them from mandatory and voluntary standards is their lack of third party verification, and a lower degree of transparency and participation by the affected stakeholders.”⁷

Whereas a lot of people are distrustful of companies and their products, most people trust standards. One important driver of distrust is lack of knowledge or rather the reluctance of most companies to be transparent about their activities.⁸ Companies tend to communicate mainly about the things they do well. They often are reluctant to provide information about the negative effects of their business activities. Standards are needed to ensure that consumers, particularly in high-income countries, can obtain complete information on products in order to make individual choices based on their personal beliefs and preferences.

Moreover, consumers need to have confidence in the value of a particular standard to be able to choose a certified or labelled product. For example, when you buy fair trade products, you must be convinced of the value of fair trade, the value of fair trade standards, and you need to trust the organisations involved in the certification of fair trade products. Likewise, if a person is considering buying timber certified by the Forest Stewardship Council FSC, he or she needs to trust the traceability system developed by the FSC.

Standards provide information with regard to social and environmental performance

Standards provide information about the social and environmental performance of goods and services, including information about the supply chain. When consumers purchase labelled or certified products, they are sufficiently convinced that they are buying sustainable, environmentally friendly, safe or high-quality products. They trust the standards rather than the product or the companies that make the product. The problem is that the systems to implement standards are never perfect. All standards have flaws.

The SA8000 standard

An example of a rather comprehensive standard is SA8000, short for Social Accountability 8000. SA8000 is a voluntary multi-sectorial standard for auditing and certifying corporate responsibility developed by US-based Social Accountability

International SAI (formerly the Council on Economic Priorities Accreditation Agency) in 1997. The standard is primarily intended for use by manufacturers and suppliers. The standard and its verification system draw from established business strategies for ensuring quality (such as those used for the ISO 9000 standard) and include several elements that international human rights experts have identified as essential to social auditing. SA8000 is based on the principles of international human rights norms as delineated in International Labour Organisation ILO conventions, the UN Convention on the Rights of the Child and the Universal Declaration of Human Rights.⁹ SAI trains and accredits social auditing firms and individual auditors who then are hired by companies to certify their own or their supplier's compliance with SA8000 standards. The SA8000 standard includes stipulations on child labour, forced labour, health and safety, freedom of association and collective bargaining, discrimination, workplace discipline, working hours, compensation and management systems.¹⁰

SA8000 is a standard for auditing and certifying responsibility

After reading this, socially-aware consumers might think: "If a brand-name company states that it sources from SA8000-certified suppliers, it must be a socially responsible company."

Unfortunately, the SA8000 system is not perfect. Research undertaken in 2005 by the Clean Clothes Campaign CCC demonstrated many weaknesses in the social auditing systems used to verify compliance with voluntary CSR standards.¹¹ Workers at an SA8000-accredited factory in China producing for, among others, fashion labels DKNY and Michael Kors said the following to the researchers: "The auditors never told the workers [...] their identity. [...] Nor did the auditors inform the interviewed workers about how the information they conveyed would be protected and how the workers could complain in case of retaliation or reporting of code violation."

In one SA8000-accredited factory in North India, workers stated that no improvements had been made in the health and safety situation in the factory since they joined the factory. In Tirupur, India, a consultant, who provided factories with advice on how to obtain SA8000 accreditation, specifically advised clients to set up welfare committees as an alternative to unions.¹²

Labour issues in SA8000-accredited factories in India

In an unprecedented legal move, Fibres & Fabrics International FFI and its subsidiary Jeans Knit Pvt. Ltd. JKPL in Bangalore accused the CCC of "cyber-crime, acts of racist and xenophobic nature, and criminal defamation." FFI was one of the companies included in the research on social auditing systems. Brands sourcing from the company include Guess, RaRe, Armani, Mexx, Gap, Ann Taylor and G-Star. In June 2006, FFI and JKPL petitioned and received a court order to prevent labour organisations and trade unions from speaking out about labour violations in the company's factories. The organisations named in the order included Munnade, CIVIDEP and the trade unions GATWU and NTUI. The court issued a temporary restraining order in July 2006, which was prolonged in February 2007. The order effectively silenced local stakeholders from speaking out about what they believed was the real labour situation and providing support to workers in improving the labour conditions at FFI and JKPL.

Restraining order silenced stakeholders from revealing labour conditions

At the same time, a fact-finding mission (formed by local legal, academic and human rights practitioners) interviewed workers and met with management. The

subsequent report was published on the CCC website in August 2006.¹³ The following allegations were in the report:

- Beatings occur for even minor faults in work and when workers cannot meet production targets that are unreasonably high.
- Supervisors themselves are beaten.
- In October 2005, a boy was stripped and beaten in front of all the workers in the shift.
- Musclemen are paid to beat up the workers outside the factory.

SAI wants to see certification of production facilities suspended

Four out of five FFI production facilities had been accredited with the SA8000 certification as of December 2006. A month earlier, the CCC filed a formal complaint with SAI, challenging the ongoing certification process of the FFI/JKPL production units. On the basis of an evaluation, SAI formally informed FFI and JKPL in writing that it would advise its certification bodies to suspend the certification of FFI and JKPL facilities unless FFI and JKPL engaged with the local labour organisations to normalise the strained labour relations. This could also include taking steps towards the lifting of the restraining order. In April 2007, SAI posted a public statement on its website which declared legal proceedings against local stakeholders to be fundamentally incompatible with SA8000 certification of companies.¹⁴

Voluntary or mandatory?

A voluntary CSR standard may be quite comprehensive, but the systems designed to ensure compliance with the standard are seldom satisfactory. Implementing policies has proven to be far more difficult than policy-making.

If even CSR standards, labels and certifications have flaws, what is a consumer to do? Companies that apply CSR standards and use these standards to communicate the credence attributes of their products are probably, but not certainly, doing better than companies that do not worry about CSR at all. We could say, paraphrasing Twain, that you know so much more of a product when all you have seen is its label. Although there are many labels and certifications, fears of confusion in the marketplace due to the proliferation of different standards seem unfounded.¹⁵ Perhaps, in the next five years, many labels, certification schemes and other sorts of voluntary standards will start converging.

Are voluntary approaches to transparency on CSR-related issues all we need?

A prelude to this trend is the work of the ISO Working Group on social responsibility. For the past three years, the International Standards Organisation ISO has been developing an international standard that will give guidance to organisations on social responsibility – the ISO 26000 standard. In order to avoid inconsistencies with and duplication of other voluntary standards and international regulations in the field of social responsibility, the ISO has signed a memorandum of understanding with the UN Global Compact and the International Labour Organisation. Other standard-setting organisations in the field of CSR, such as the Global Reporting Initiative GRI and Social Accountability International, have not signed memorandums of understanding with the ISO, but have actively participated in the process.¹⁶

Transparency through the use of voluntary CSR standards should be encouraged. But are voluntary approaches to transparency on CSR-related issues all we need? On the one hand, the European Commission states in its 2006 communication that it will examine the need for further voluntary actions to achieve the objective of transparency and information for consumers. On the other hand, the commission says that, in spite of all the voluntary standards that have already been created, “consumers lack clear information on the social and environmental performance of goods and services, including information on the supply chain.”¹⁷

Does this mean that there are limits to voluntary transparency? Many NGOs and trade unions think there is a need to move beyond voluntary compliance. They believe that regulatory measures are necessary to complement the many voluntary CSR initiatives and have called on the EU to take the lead in the development of an effective European CSR framework. Such a framework would have to be based on internationally agreed standards and principles, such as the OECD guidelines and the conventions of the ILO, and should involve all stakeholders from the early stages of development and include credible provisions for monitoring and verification.¹⁸ The European Coalition on Corporate Justice ECCJ, a network of civil society organisations from across Europe, recommends the following measures to improve transparency:

- Mandatory social and environmental reporting;
- Disclosure of payments and lobbying vis-à-vis public authorities;
- A right for consumers and other stakeholders to know about social and environmental conditions in production processes, products and services.¹⁹

Not only NGOs and trade unions have emphasised the need for governmental regulation in relation to transparency. Achim Steiner, UN under-secretary-general and executive director of the UN Environment Programme UNEP, recently stated that it is the *right time* for governments to introduce mandatory CSR reporting: “We need to liberate business by providing it with the regulation that it needs to do something differently. To set regulatory frameworks is exactly what is needed now.”²⁰

Voluntary CSR standards should thus be complemented by mandatory standards. A balanced mix of both is likely to benefit transparency and increase the possibilities for consumers to exercise critical choice. Governments need to take up the responsibility to regulate corporate social responsibility. Although it is clear that regulation by itself cannot provide all the answers, governments, the EU government in particular, could help lead the way to good products and good companies. It may be an arduous task to create mandatory standards but consumers will benefit greatly. ♦

Voluntary and mandatory CSR standards likely to increase transparency

Notes

- ¹ Quote attributed to Mark Twain, in: Flannery (ed.), *The Birth of Sydney: The story of Britain's arrival in the antipodes*, London, 2003, p. 319.
- ² *Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee – Implementing the partnership for growth and jobs: Making Europe a pole of excellence on corporate social responsibility*, Commission of the European Communities, Brussels, March 22, 2006, p. 7. URL: <<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52006DC0136:EN:NOT>>.
- ³ *Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee – Implementing the partnership for growth and jobs: Making Europe a pole of excellence on corporate social responsibility*, Commission of the European Communities, Brussels, March 22, 2006, p. 7. URL: <<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52006DC0136:EN:NOT>>.
- ⁴ Hohnen, *Transparency: The path to 'clearly better' sustainability and performance*, paper for the 9th International Energy Forum, Amsterdam, 2004, p. 3.
- ⁵ Comment by Chinyere Almona during an e-discussion organised by the International Finance Corporation, May 10, 2004.
- ⁶ Comment by Monica Araya during an e-discussion organised by the International Finance Corporation, May 12, 2004.
- ⁷ Ponte, *Standards and Sustainability in the Coffee Sector: A global value chain approach*, International Institute for Sustainable Development, Winnipeg, 2004, pp. 7-8.
- ⁸ Henriques, *Corporate Truth: The limits to transparency*, Earthscan, London, 2007, p. 127.
- ⁹ Hohnen, *Corporate Social Responsibility: An implementation guide for business*, International Institute for Sustainable Development, Winnipeg, 2007, p. 101.
- ¹⁰ Slob & Oldenziel, *Coffee & Codes*, SOMO, Amsterdam, 2003, p. 38.
- ¹¹ Pruett et al., *Looking for a Quick Fix: How weak social auditing is keeping workers in sweatshops*, Clean Clothes Campaign, Amsterdam, 2005.
- ¹² Pruett, *Looking for a Quick Fix: How weak social auditing is keeping workers in sweatshops*.
- ¹³ Devraj et al., *Fact Finding Report of Violation of the Rights of Workers at Washing Unit of Fibre & Fabrics International Pvt. Ltd. (FFI), Peenya Industrial Area*, Bangalore, 2006.
- ¹⁴ CSR Asia Weekly, Vol. 3, Week 33, August 15, 2007.
- ¹⁵ Rice & McLean, *Sustainable Coffee at the Crossroads*, paper prepared for the Consumer's Choice Council, October, 1999. URL: <<http://www.greenbeanery.ca/bean/documents/sustainableCoffee.pdf>>.
- ¹⁶ Slob & Oonk, *The ISO Working Group on Social Responsibility: Developing the future ISO SR 26000 standard*, briefing paper, SOMO, Amsterdam, 2007.
- ¹⁷ *Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee – Implementing the partnership for growth and jobs: Making Europe a pole of excellence on corporate social responsibility*, Commission of the European Communities, Brussels, March 22, 2006, p. 7. URL: <<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52006DC0136:EN:NOT>>.
- ¹⁸ Oldenziel, *European Commission Abandons Multi-stakeholder Approach in CSR*, Ethical Corporation, April, 2006, p. 15.
- ¹⁹ Oldenziel (ed.), *Corporate Social Responsibility at the EU level: Proposals and recommendations to the European Commission and the European Parliament*, ECCJ, Brussels, 2006.
- ²⁰ Russell, *Europe: Public policy - Red tape back in fashion?*, Ethical Corporation, November, 2006. URL: <<http://www.ethicalcorp.com/content.asp?ContentID=4620&rss=36.xml>>.