

ETI Forum



Purchasing Practices

***Case studies to address
impacts of purchasing
practices on working
conditions***

Report from ETI members' meeting, 29 November 2007

About ETI

The Ethical Trading Initiative (ETI) exists to identify and promote good practice in the implementation of codes of labour practice, including the monitoring and independent verification of code provisions. We are an alliance of companies, trade union organisations and non-government organisations (NGOs) committed to working together to achieve that aim. Our ultimate goal is to ensure that the working conditions of workers in companies that supply goods to consumers in the UK meet or exceed international standards.

The ETI Base Code is founded on International Labour Organisation (ILO) Conventions and has become a model on which other codes are based. ETI's Base Code can be seen in full on our website (www.ethicaltrade.org).

We were established in 1998 as an independent, not for profit organisation. We are funded by member contributions and a grant from the UK Department for International Development (DFID).

About ETI Forum

ETI Forum reports on the key issues discussed at one of our events. ETI events – members' roundtables, public seminars and conferences – focus on ethical trade issues of topical interest or which have proved to be particularly challenging to our members. For example, we have held events on freedom of association and collective bargaining, getting smarter at auditing, corrective actions in code compliance and the role of gangmasters in the food and agricultural industry. These events give members and others the opportunity to learn from guest speakers and from each other, and to debate practical responses to the issues raised.

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About this report

This report sets out some of the key issues presented and discussed at the ETI members' meeting on 29th November 2007. The meeting provided a forum for members to explore potential solutions to some of the common purchasing practices which undermine working conditions in the supply chain. The meeting comprised presentations and workshops, during which members discussed real-life examples of purchasing practices and their impacts. This report includes details of the case studies discussed during the meeting, along with the possible solutions identified by members. It also sets out how the case studies could be used as a practical tool to help improve purchasing practices along supply chains.

Who is this report for?

This report is aimed specifically at:

- Retail staff with commercial responsibilities, with responsibility for purchasing, and/or with responsibility for ethical trade.
- Retail staff working with buying teams and/or suppliers to review and improve purchasing practices.
- Suppliers who want to engage with retailers to find solutions to some of the negative impacts associated with purchasing practices.
- Trade unions and NGOs who are working with companies to address purchasing practices.

Purpose of this report

This report aims to serve as an aide memoire for those who attended the members' event. It is also intended to provide a tool for:

- raising awareness of the various impacts of purchasing practices amongst key buying staff within retailers; and
- helping key buying staff to explore practical solutions to some of the purchasing practices that undermine labour standards.

Background and purpose of the event

It is increasingly recognised that retailers' purchasing practices can have a significant negative impact on working conditions in the supply chain. Many key purchasing processes and decisions within a sourcing company – such as critical path management, terms and conditions in the buyer-supplier relationship, sourcing and merchandising – affect how suppliers manage their workforce and production, and can indirectly impact on working conditions. This is supported by findings of the ETI Impact Assessment (2006) which found that '... suppliers in all countries and sectors reported that [downward pressure on prices and lead times] limited their ability to make improvements in labour practices'.

Since 2005, the ETI Purchasing Practices Project has been working to tackle these issues and identify purchasing practices which support a company's commitment to labour standards. The Project Group includes several member companies, trade unions and NGOs working together to assess the impacts of buying practices throughout the supply chain. As a result of taking part in the project, some participants have been able to make recommendations for changes to buying practices, have communicated these to company Boards, and begun a training programme for buying staff. The aim is to disseminate the learning from the Purchasing Practices Project Group in order to help all ETI company members integrate ethical trading into core business practices.

It is against this background that ETI held a members' meeting to explore potential solutions to some of the common purchasing practices which undermine working conditions, and to encourage companies to consider what practical improvements they can make in their own buying processes.

Who participated

More than 100 people attended this event, comprising over 60 participants from ETI member companies including staff from buying departments, 14 NGOs, 12 trade unions and ETI secretariat staff. This large turnout is testament to the importance of purchasing practices to the ethical trade agenda.

1 Exploring purchasing practices through case studies

1.1 Case studies on purchasing practices

The members' meeting started with open and honest presentations from company and trade union members about some of the ethical issues in purchasing practices, and ways in which these could be addressed.

Following this, members took part in tripartite workshops (with representatives from companies, NGOs and trade unions) in which they discussed real-life examples of the ways in which retailers' purchasing practices are impacting on workers, and explored how retailers – working in collaboration with suppliers – could resolve these types of problems.

Three case studies were used as the basis for the workshops. Each case study described the impact of a particular purchasing practice – downward pressure on prices, last minute ordering, or lack of integration between commercial and ethical activities – which commonly occur in retail companies.

For each of the case studies, members explored the following key issues:

- what breaches of the ETI Base Code occurred in the case study scenario and possible impacts on workers;
- how, if at all, the buying practices described go against the ETI Principles of Implementation;
- the factors that led to the breach occurring; and
- what could be done to prevent that kind of breach happening again.

1.2 Using the case studies

The case studies proved a useful way of helping participants to identify and highlight the issues and impacts associated with particular purchasing practices, and to discuss possible ways of addressing these.

The following sections set out the case study scenarios, and the issues and solutions suggested by members during the workshops. It is intended that by including the information here, the case studies and associated information can be used as a practical tool by retailers, suppliers, Trade Unions and NGOs in their work to address some of the negative impacts of purchasing practices and improve conditions for workers along the supply chain.

2 Case Study A: Exerting downward pressure on prices

2.1 The case study scenario

Members were presented with a case study of a situation whereby a retailer plans to cut costs by reducing prices paid to suppliers.

Context: Part of the 2007 merchandising strategy in a major high-street clothing retailer is to cut costs in the supply chain by reducing prices paid to suppliers by 5% on previous year's factory gate prices. All merchandisers in the business are informed of this target, and are instructed to negotiate with suppliers to reduce factory gate prices for comparable products to 5% lower than in 2006. Individual merchandisers are told that they will be rewarded for meeting cost-cutting targets with a performance-related bonus at the end of the year.

Buying practice: Merchandisers based in India negotiate with long-standing suppliers to achieve the lower price, and assure suppliers that they will get repeat orders over the next year if they can meet this lower price. The suppliers agree.

The supplier and worker scenario: One factory manager calculates that, if they produce the goods in their own factory, the lower price means that they will only just break even. This is because the unpredictable flow of orders with short lead times will require them to do overtime shifts, and the costs of paying overtime premiums will be too expensive. Therefore, to keep costs down, the factory manager decides to sub-contract part of the order to another factory in the city which has lower operating costs, without telling the retailer. The sub-contractor has never been audited and does not know about the ETI Base Code standards. Workers at the sub-contractor's factory are paid below the legal minimum, working hours often exceed 60 hours a week, and none of the workers have contracts. There are no fire exits in the factory.

2.2 Impacts along the supply chain

Members discussed the case study and explored the way in which the retailer's actions might affect working conditions along the supply chain. A number of impacts were identified, as set out below.

Impacts on workers

The retailer's practice of reducing the price paid to suppliers has a range of impacts on workers and results in a number of breaches of the Base Code along the supply chain. For example, in one factory, the following breaches occur:

- Wages fall below a living wage.
- Regular employment is not provided.
- Excessive working hours are imposed.
- Working conditions are not safe (there are no fire exits).

Breaches of ETI's Principles

The retailer's buying practices also go against ETI's Principles of Implementation (PoI). In particular, the following Principles are not applied:

- The code and the implementation process are not integrated into the core business relationships and culture (PoI 1.4).
- Negotiations with suppliers do not take into account the costs of observing the code (PoI 5.1).
- Understanding and implementation of company policy with respect to its code of labour practice do not constitute a positive performance measure for personnel (PoI 5.2).

2.3 What went wrong?

From the information given, it appears that a number of factors led to these breaches occurring. These include:

- The merchandising strategy does not take the costs of production into account.
- Ethical objectives are not integrated into the buying team's roles.
- The factory manager accepts the lower price without bargaining – possibly because of the retailer's more powerful bargaining position and possibly because of oversupply in the industry.
- There is no discussion between the retailer and factory manager about how to deliver the order at the lower price.
- There is illegal sub-contracting (without telling retailer) and therefore no audit of the sub-contractor.

2.4 What could be done in future?

ETI members identified a range of measures that retailers, in conjunction with suppliers, could adopt to prevent this kind of breach occurring in future. This is not an exhaustive or prioritised list, but a set of potential solutions which individual companies would need to explore for themselves.

2.4.1 Involve the Board

Communicate the impacts of purchasing practices to the Board and seek support from the Board for initiatives to review purchasing practices.

2.4.2 Train key staff

Train key retail staff, such as merchandisers and buyers, so that they are aware of the potential impacts of their decisions on suppliers and workers.

2.4.3 Model production costs

Ensure that managers model the costs of production when setting their merchandising strategy.

2.4.4 Adopt alternative cost-cutting strategies

Encourage buying teams to consider other ways to cut costs rather than negotiating factory gate price reductions. For example, buyers could:

- Seek ways to reduce the level of sampling.
- Work with factories to improve efficiency over time.
- Work with designers and technologists to model the costs of production at the design stage.

2.4.5 Amend job descriptions

Include the following responsibilities in the job descriptions of relevant buying staff:

- Check production capacity in the factory.
- Estimate production costs and take estimates into consideration when negotiating with suppliers.
- Discuss with factory managers how they will meet orders without breaching the Base Code.
- Ask suppliers for transparency on sub-contracting.

2.4.6 Improve cross-team working

Improve working relationships between ethical trade staff/teams and commercial staff/teams in retail companies, in order to:

- Share information on suppliers with better labour practices.
- Improve understanding of commercial practices.
- Provide better support for commercial teams to address purchasing practices.

2.4.7 Raise consumer awareness

Educate consumers about the complexity of supply chains and working conditions.

2.5 Notes on implementation

Members noted a number of caveats to the solutions proposed during the workshop discussion. In particular, it was noted that:

- Expanding the role of buying staff will increase their workload, and they may need additional resources to take on such work on a long-term basis.
- It may take time to build sufficient trust between factory managers and customers, before factory managers feel able to hold open and honest discussions on production capacity, costs and sub-contracting.

3 Case Study B: Last minute ordering

3.1 The scenario

Members were presented with a case study in which buyers regularly amend daily orders and sometimes cancel orders altogether.

Context: A farm in Kenya produces fresh produce for a UK retailer. The farm has an annual contract with the retailer. Produce is flown overnight every night to be on the shelves for the next day. The farm has thousands of workers whose families rely on the income that is generated through this work.

Buying practice: The UK buyer forecasts orders on a weekly basis. However, the daily requirements are amended throughout the week according to daily sales data, UK weather, promotional competition and department wastage targets. On average, orders are revised (up or down) three days a week and the change is faxed through to the supplier by mid-afternoon. The changes in volume are often around 50% more or less than the forecast. When demand is sufficiently low, the order is cancelled altogether (this happens approximately ten times a year).

The supplier and worker scenario: Any changes to the daily order are received at the grower's packhouse in the late afternoon.

If the order is increased, underproduction is addressed by asking workers to do overtime. Women workers rely on company transport to take them home because it is unsafe to walk and, as buses do not leave until the later shift is finished, many workers have little choice but to continue working overtime. Furthermore, supervisors sometimes intimidate the women to stay and help meet the order. As a result, people who work in the packhouse have to work longer hours in cold conditions to meet the increased order. In addition, the farm manager is unable to negotiate a higher price for the additional stock, and so does not pay the workers a higher hourly rate for overtime.

If the order is decreased or cancelled, the lost revenue has to be factored into the suppliers' costs. As a result, the supplier sends workers home early and does not pay them fully for the hours worked.

3.2 Impacts along the supply chain

Members discussed the case study and explored the way in which the retailer's ordering practices might affect working conditions along the supply chain. A number of impacts were identified, as set out below.

Impacts on workers

The retailer's practice of changing orders at short notice results in a number of breaches of the Base Code, including the following:

- Workers experience harsh or inhumane treatment (intimidation to stay and finish order from supervisors).
- Forced overtime occurs (without buses there is no safe means of leaving the worksite).

- There is no premium for working overtime.
- There is non-payment of wages (when orders are cancelled).
- Working conditions are not safe (longer working in the cold store).

It also appears that freedom of association and collective bargaining are not taking place on this site.

Breaches of ETI's Principles

The retailer's buying practices also go against the Principles of Implementation (PoI). In particular, the following Principles are not applied:

- The code and the implementation process are not integrated into the core business relationships and culture (PoI 1.4).
- Negotiations with suppliers do not take into account the costs of observing the code (PoI 5.1).

3.3 What went wrong?

From the information given, it appears that a number of factors led to these breaches occurring, including the facts that:

- There is fluctuating consumer demand.
- The retailer and supplier have not agreed a minimum order value or volume, which means that significant order reductions or cancellations can occur without compensation.
- No notice is given to suppliers for changes to orders.

It also appears that there is no collective bargaining of workers with the employer to agree overtime, transport and shift arrangements.

3.4 What could be done in future?

ETI members identified a range of measures that retailers, in conjunction with suppliers, could adopt to prevent this kind of breach occurring in future. This is not an exhaustive or prioritised list, but a set of potential solutions which individual companies would need to explore for themselves.

3.4.1 Raise awareness among buyers

Raise awareness amongst buyers of the impact their decisions have on suppliers. Emphasise the importance of making changes as early as possible (eg the day before) so that workers have notice and can volunteer for overtime.

3.4.2 Agree minimum orders

Set out minimum order volumes or values with suppliers to give more stability to the supplier.

3.4.3 Model wastage costs

Work with suppliers to find ways of reducing waste, model the cost to the producer of unavoidable waste, and build this in to retailers' cost models.

3.4.4 Improve forecasting

Explore improvements to forecasting, such as:

- Sharing real-time sales data with suppliers.

- Where possible, holding buffer stocks in cold storage to deal with peaks in demand.
- Researching the peaks and troughs of demand to identify any improvements that can be made to forecasting systems.
- Training forecasters to ensure they are using the best available forecast methods.

3.4.5 Encourage actions by suppliers

Members also identified a number of actions that could be taken by suppliers, including:

- engaging with workers to explore solutions, such as setting up shift patterns; and
- making buses available for workers to leave at the end of the standard working day, as well as at the end of an overtime period.

4 Case Study C: Lack of integration between commercial and ethical activities

4.1 The scenario

Members were presented with a case study in which there is a lack of integration between the activities of a retailer's audit team and its buyers.

Context: A high-street retailer buys basic T-shirts all year round and often sources from the same factory in Bangladesh. The retailer has commissioned audits of this factory and the factory manager has made efforts to follow the corrective action plans. Working conditions have improved over time, particularly regarding health and safety, and a newly established worker committee has met with management and successfully bargained for wages above the national minimum wage. The buyer's performance is largely measured against sales and margin targets.

Buying practice: A large order for T-shirts is about to be placed. The buyer asks for quotes from several factories, all of which operate to good quality and service levels. The factory that usually supplies the T-shirts tenders at \$1.50 per item, which is the same price as the previous year; a neighbouring factory tenders at \$1.40. The buyer uses the lower quote to try and bargain the price down at the usual factory, but the factory manager refuses to reduce the unit price. As a result, the order is placed with the cheaper factory.

The supplier and worker scenario: An audit of the new (cheaper) factory is carried out after the order is placed there. The audit finds no mention of a trade union or collective bargaining in the factory, and pay records show that most workers are paid the national minimum wage.

4.2 Impacts along the supply chain

Members discussed the case study and explored the way in which the retailer's actions might affect working conditions along the supply chain. A number of impacts were identified, as set out below.

Impacts on workers

The retailer's lack of integration of commercial and ethical objectives results in a number of breaches of the Base Code, including the following:

- There is no freedom of association or the right to collective bargaining.
- Wages fall below a living wage (the Bangladesh minimum wage is commonly known to be less than a living wage).

Breaches of ETI's Principles

The retailer's buying practices also go against the Principles of Implementation (PoI). In particular, the following Principles are not applied:

- The code and the implementation process are not integrated into the core business relationships and culture (PoI 1.4).
- Negotiations with suppliers do not take into account the costs of observing the code (PoI 5.1).

- Understanding and implementation of company policy with respect to its code of labour practice do not constitute a positive performance measure for personnel (PoI 5.2).

4.3 What went wrong?

From the information given, it appears that a number of factors led to these breaches occurring. These include:

- A lack of collaboration and/or communication between the managers of the audit programme and the buying teams at the retailer.
- Ethical factors are not included in merchandiser's decision making or performance management.
- There is a strong focus on cutting cost, perhaps below a level at which a supplier can meet ethical standards.

4.4 What could be done in future?

ETI members identified a range of measures that retailers, in conjunction with suppliers, could adopt to prevent this kind of breach occurring in future. This is not an exhaustive or prioritised list, but a set of potential solutions which individual companies would need to explore for themselves.

4.4.1 Train buying staff

Train buying staff on the following:

- The value of mature industrial relations.
- Country-specific labour issues (eg level of minimum wage).
- The complexity and stages in the supply chain, including sourcing of inputs, production and outsourcing.
- How to factor in ethical standards and ask related questions of suppliers.

4.4.2 Use approved supplier lists

Introduce a list of approved suppliers who have a track record in improving labour standards. As well as reducing the risk of sourcing from unknown suppliers, this provides an incentive for suppliers to improve labour standards in order to join the approved list.

4.4.3 Share audit reports with buyers

Ensure buyers are aware of all audit reports so that they develop awareness of labour issues in the supply chain, and can begin to discuss these issues with their suppliers.

4.4.4 Increase accountability among buying staff

Hold buying staff accountable for the labour standards in their supply base and develop appropriate performance indicators.

4.4.5 Consider wider cost implications of decisions

Consider the wider cost implications (beyond factory gate prices) of shifting orders to new suppliers, such as the costs of working with new suppliers to meet technical requirements.

4.4.6 Raise awareness

Educate store staff and consumers about the implications of low-cost products (eg T-shirts or food items), so that:

- consumers become aware of the 'human cost' of low prices and start to question extremely low prices; and
- marketing staff can promote the wider benefits of products (rather than being engaged in a race to the bottom on price alone).

5 Next steps

These case studies can be used as a starting point for a review of purchasing practices in any business. For example, companies can:

- Set up workshops with senior managers and buying teams, and use the case studies as a way of discussing or raising awareness of how purchasing practices can impact on workers and potential solutions to issues identified.
- Draft their own case study scenarios, and explore potential impacts down supply chains through conversations with suppliers and workers.
- Start a discussion between buying teams and their suppliers about where there is room for improvement in buying practices.

Feedback on how the case studies are being used, additional solutions identified, or the development of new case studies should be sent to the ETI Purchasing Practices Project Manager, Miriam Neale (Miriam@eti.org.uk).

6 Further information

ETI

The following documents are available on the ETI website at www.ethicaltrade.org

- ETI Base Code and Principles of Implementation.
- *Bridging the Gap Between Commercial and Ethical Trade Agendas: Pioneering Approaches to Purchasing Practices*, Briefing Paper No 5, ETI, 2005.
- ‘Purchasing practices: what impact on labour conditions?’, Chapter 9 of *Key Challenges in Ethical Trade: Report on the ETI Biennial Conference 2003*, ETI, 2003.
- *Purchasing practices: Marrying the Commercial with the Ethical*, ETI Members’ Roundtable, 7 July 2004.
- *Key Challenges in Ethical Trade: Report on the ETI Biennial Conference 2003*, ETI Report, 2003.

Further details on training buyers can be found at www.ethicaltrade.org/d/purchasingpractices.

Information on ETI’s Purchasing Practices project can be found on the ETI website, or from the ETI Purchasing Practices Project Manager, Miriam Neale (Miriam@eti.org.uk).

Acona/Insight Investment

Buying Your Way Into Trouble? The Challenge of Responsible Supply Chain Management, Insight Investment in conjunction with Acona, available to download at www.insightinvestment.com.

ILO

All International Labour Organization (ILO) Conventions and Recommendations can be found in full on the ILO website at www.ilo.org.

Oxfam

Trading Away Our Rights: Women Working in Global Supply Chains, Oxfam, 2004, available for download at www.publications.oxfam.org.uk

Traidcraft

Buying Matters. Consultation: Sourcing Fairly from Developing Countries, Traidcraft, 2006, available to download at www.responsible-purchasing.org.

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