

Supplier review: approaches and perspectives

Application note

A key component in respecting corporate due diligence is supplier management. Once you have informed suppliers of your expectations, based on a code of conduct, it is important to check whether these expectations are being met. There are several approaches available for this.

This practical guide is intended to help you to become familiar with the characteristics of existing approaches and to be able to classify them in order to be able to select an approach that is suitable for your company on this basis. In addition, the practical guide is intended to support you in identifying requirements that arise from your own role as a supplier.

Review suppliers and implement customer requirements: Why it is important to understand both perspectives

Your suppliers are important partners in identifying and addressing risks along the value chain. The basis of supplier management is to start a dialogue. Suppliers are partners when it comes to making supply chains more sustainable. The basis for jointly developing a sustainable supply chain is to review implementation status: Do your suppliers meet the requirements you have formulated? What gaps or even shortcomings are there? Getting answers to these and other questions is important so that corrective and improvement measures can be developed and implemented. It also helps suppliers to improve their sustainability performance.

At the same time, many small and medium-sized enterprises (SMEs) are suppliers of companies that formulate sustainability requirements. In the course of the implementation of the German Supply Chain Due Diligence Act (LkSG), companies falling within the scope of the law are likely to impose specific requirements on to their direct suppliers to comply with their own due diligence obligations. This trickledown effect has an impact on many SMEs. They should therefore prepare as soon as possible to understand the (increased) requirements and work together with their clients to establish appropriate due diligence processes.

Central contents

In the following, two key perspectives of supplier management from an SME's point of view are captured:

- The perspective of a company that has a responsibility to respect human rights and environmental standards along **its supply and value chains** and to implement appropriate measures (see [Perspective 1: Review own suppliers](#)).
- The perspective of a company that must comply with **customer requirements** and in turn be able to establish due diligence processes (see [Perspective 2: Being verified as a supplier by customers](#)).

Perspective 1: Review own suppliers

1. Risk analysis and dialogue as a basis for supplier review

Supplier review should always be embedded in a broader dialogue:

- Clearly communicate to your suppliers the expectations you have set out in a code of conduct. The goal you are pursuing with the code of conduct must be sufficiently clear to suppliers.
- In addition, communicate how your company can support suppliers and the benefits that engagement can have for suppliers.
- Make it clear that when deviations from these requirements occur, it is about improving supplier performance, not terminating the supplier relationship. Hence, communicate clearly what will happen if suppliers do not comply with your requirements.
- Having said that, supplier reviews always require a certain effort. For example, self-declarations of suppliers must be evaluated by your company. Therefore, you should make an informed decision about which suppliers you want to review and how it is done.
- Use the results of your risk analysis to target individual suppliers for an in-depth review. For example, you should review suppliers with a higher priority in more detail than those for whom you have identified fewer risks.
- Follow up on implausible or incomplete responses from suppliers.

2. Approaches to supplier reviews: self-assessment and on-site verification/audit

In practice, companies often use two approaches to supplier verification:

- Self-assessment
- On-site inspections or audits.

Both approaches differ, among other things, regarding the level of detail of the assessment and its respective effort. This leads to certain advantages and disadvantages. You should therefore consider carefully which approach to follow with each supplier. Sometimes it makes sense to group suppliers together.

Both approaches should be integrated into management processes that have been or are being established to implement corporate due diligence. The two approaches can also be combined.

Supplier audits are important sources of information for the human rights and environmental risk analysis. On-site visits can be integrated into existing purchasing processes and activities that take place directly at supplier production sites.

| | Self-declaration | On-site inspection / audits |
|--------------------|---|---|
| Description | <p>What should be considered?</p> <ul style="list-style-type: none"> • Self-declarations are used to give customers a better picture of whether suppliers are complying with the standards set out in codes of conduct/contracts. • For example, proof of certification (e.g. ISO 14001, EMAS, etc.) or management approaches can be requested. • The existence of sustainability certificates for raw materials and products (particularly relevant for retailers and processing companies) can also be checked. • Self-declarations may include both company-related and site-related information. • Self-declarations should be repeated at regular intervals (e.g. 1x per year). • Self-declarations can also be used to verify the direct supplier's approaches to reviewing its upstream suppliers. • Too many closed questions that can only be answered with yes/no should be avoided (low knowledge gain). | <p>What should be considered?</p> <ul style="list-style-type: none"> • A distinction must be made between on-site inspections by your own employees and audits by independent auditors. <p>On-site inspections:</p> <ul style="list-style-type: none"> • Random on-site visits (e.g. in conjunction with other appointments) can be used to verify self-declarations. • On-site audits can ensure that identified problems along the supply chain have been addressed as part of the due diligence process. <p>Audits:</p> <ul style="list-style-type: none"> • An audit is a "systematic, independent and documented process for obtaining audit evidence and evaluating it objectively to determine the extent to which audit criteria are fulfilled (ISO 19011:2011). • Audits serve as third-party verification that due diligence processes are in place and that the company is continuously improving its supply chain management. |
| Advantages | <p>Why self-declarations?</p> <ul style="list-style-type: none"> • Self-declarations serve as an initial assessment of suppliers' compliance with environmental and social standards. • Self-declarations can make suppliers aware of risks. • Self-declarations are a good basis for further reviewing tools such as on-site visits or audits. | <p>Why on-site inspections?</p> <ul style="list-style-type: none"> • Use the on-site impression to verify the results of the self-declaration and obtain evidence of good or insufficient supplier performance. • Personal observations as a basis for in-depth exchange (including competence building). <p>Why audits?</p> <ul style="list-style-type: none"> • Strengthening the credibility of audit results when carried out by external auditors. • If capacities /know-how are lacking, audits by external third parties are advisable. |

| | Self-declaration | On-site inspection / audits |
|----------------|--|---|
| Disadvantages | <ul style="list-style-type: none"> • Preparation and translation efforts by writing questionnaires in the national language are costly. • Translation of answers in the national language is time-consuming. • Provision of knowledge and human resources for the evaluation of self-declarations are necessary, but not always available. • Additional effort is needed if answers are incomplete or not plausible. | <ul style="list-style-type: none"> • Limited to snapshot of situation on the ground; there is a risk that regular processes will not be captured. • Time- and cost-intensive preparation, implementation and evaluation, for which human and/or financial resources must be expended. • The preparation and review of corrective action plans can be overwhelming, especially for smaller companies. |
| Classification | <ul style="list-style-type: none"> • A self-declaration is an initial assessment of the status quo of suppliers. • A self-declaration is often the first step in the implementation of a supplier code of conduct or the introduction of new suppliers. | <ul style="list-style-type: none"> • Audits serve to verify specific sustainability standards. • Audits are particularly suitable for checking suppliers who are at increased risk of non-compliance. • The on-site review can be carried out by the company's own staff; however, the review is not to be equated with an audit. |

Further information:

- Information in the table is largely taken from the guide "[Sustainable supply chain management for medium-sized companies in the chemical industry](#)" (English version available) by Chemie³ (p, 28ff.; prepared by Schlange, Zamostny & Co.).

Industry solution and cross-industry approaches

Both approaches – self-declaration and on-site inspections/audits – require trained personnel. It is therefore legitimate to consider whether supplier reviews can be carried out as part of an industry solution or multi-stakeholder initiative or a cross-industry supplier platform.

Industry solutions or multi-stakeholder initiatives

Industry-level or multi-stakeholder solutions offer the possibility that a supplier's assessment can be made available to multiple customers. This saves time and human resources on both sides and avoids multiple assessments and multiple audits. Costs are usually shared by member companies. Here are some examples:

- [Together for Sustainability \(TfS\)](#)
- [Drive for Sustainability](#)
- [Responsible Business Alliance](#) (formerly Electronic Industry Citizenship Coalition).

Cross-industry supplier platforms

A number of (commercial) providers, such as Ecovadis, NQC, Sedex Global or Achilles, offer companies the opportunity to use existing criteria catalogues for suppliers and supplier ratings. Among other things, platforms offer their own evaluations of suppliers, which your company can use directly or as a basis for its own evaluation.

Further information

- An overview of industry and multi-stakeholder initiatives can be found on the [CSR Practice Days website](#).
- Information on the advantages and disadvantages of industry solutions can be found in the Chemie³ guide "[Sustainable supply chain management for medium-sized companies in the chemical industry](#)" (English version available) (p. 30).

3. Self-declaration: What should your company pay attention to?

- **The prioritization of suppliers** enables you to select the most important suppliers (measured by purchasing volume, country risk, etc.) for relevant topics (environmental/social standards).
- **Communication and education about goals and the process of the self-declaration** involve the supplier more strongly in their own sustainability management. The aim is for the supplier to address sustainability issues themselves and develop their own initiatives. In return, your company can also support suppliers in integrating sustainability issues into their businesses, e.g. through training.
- **Systematic questionnaires** facilitate the targeted query of relevant aspects and enable the comparison of suppliers in the supplier evaluation. They also facilitate a uniform supplier evaluation based on a risk analysis as well as simplified decision-making processes regarding next steps (audit; measures; termination).

4. Audit: What should your company pay attention to?

- **Prioritizing suppliers** to be audited based on a prior risk assessment (e.g., based on self-declaration, country and industry risk, or for a suspected case) is important because audits are typically time-consuming and costly.
- **Communication and education about the objectives and process of the audit** promote understanding of your suppliers. The aim is that the supplier is made aware of grievances, and solutions are worked out to remedy them and, in addition, opportunities arising from improved performance are also identified.
- **Auditors** can be trained internal employees of the customer as well as independent third parties. Technical, language, industry and country knowledge are important. The advantage of external, independent auditors lies in their external credibility vis-à-vis your company's stakeholders.
- **Systematic audits**, possibly only on specific sustainability topics or certificates, facilitate the targeted retrieval of relevant information. They also enable a structured evaluation of the audit results. On this basis, informed decisions can be made about the next steps and audit results of suppliers can be compared over time.

Knowing the limitations of audits, promoting suppliers and building competencies

Audits are generally based on the assumption that suppliers are unwilling to implement customer requirements and that a control approach is therefore necessary. Study results and practical experience of companies indicate that suppliers usually want to implement requirements but are not able to do so or need incentives.

Incidents such as the Rana Plaza collapse in Bangladesh in 2013, the Ali Enterprises fire in Pakistan in 2012, and the dam failure at a retention pond at the Vale iron ore mine near the small town of Brumadinho have also tragically drawn attention to the shortcomings of (social) audits and the dramatic impacts on people and the environment, leading to a debate about the effectiveness of audits.

Research and corporate experience have shown that supply chain conditions can only be improved if suppliers recognize the need for change and the benefit to their business. Therefore, supply chain management should focus on building the competence of suppliers. Promoting factors are long-term supplier relationships and investments for structural changes in the supply chain.

The German government's [Helpdesk on Business & Human Rights](#) can provide advice on identifying suitable capacity-building measures.

Sources:

- Guide "[Doing Business with Respect for Human Rights](#)" by Shift, Global Compact Network Netherlands and Oxfam (in English)
- [Beyond Social Auditing](#)" Business & Human Rights Resource Centre blog (in English).

Promotion and financing instruments for the development of competence at suppliers

With develoPPP.de, the Federal Ministry for Economic Cooperation and Development (BMZ) promotes private-sector activities where entrepreneurial opportunities and the need for development policy action are combined. To this end, the BMZ provides financial and technical support within the framework of specific projects to companies wishing to establish or expand their involvement in developing and emerging countries. The projects funded via develoPPP.de can be used for activities in different sectors and thematic fields.

Environmental and human rights due diligence along the supply chain is becoming increasingly important. Accordingly, many companies are developing and implementing innovative and diverse solutions to improve social and environmental standards at their suppliers and subcontractors as part of the develoPPP.de programme. The BMZ contributes up to 50 per cent of the total costs under the develoPPP.de programme, with funding ranging from 100,000 to 2 million euros.

Project examples:

- [develoPPP project: BlutsGeschwister and DEG -develoPPP](#)
- [develoPPP Project: Salcomp Manufacturing and DEG - develoPPP](#)

5. Next steps

The results of the supplier review should be incorporated into the supplier evaluation and purchasing decisions:

- Based on the results and findings of self-declarations and audits, deviations from the required set of rules can be derived.
- Define a set of criteria for these variances to define different levels of severity.
- Define a zero-tolerance baseline, i.e. deviations which, if proven, will result in your company terminating the business relationship and, if necessary, drawing further (e.g. legal) consequences.
- Based on the seriousness of the infringements, a classification of the suppliers should be made.
- In each case, it is necessary to determine the consequences of the assessment, i.e. what measures are to be taken or whether the supplier is to be excluded altogether.
- Even though corrective actions and the scope with (serious) violations are important topics: To improve the supply chain, the most effective long-term approach is to build appropriate capabilities among suppliers. This will enable your suppliers to meet the expectations of the buyers.
- Participation in industry initiatives makes sense to find solutions for supplier management together with other companies (from the industry), to promote exchange as well as to improve ecological and social framework conditions in the supply chains.

Perspective 2: Being reviewed as a supplier by customers

Supplier audits are important for the customer to ensure sustainability standards in the supply chain and to select and develop suppliers accordingly. Suppliers should therefore strive to comply with sustainability standards to maintain or even expand contractual relationships as well as to gain economic advantages.

In addition, suppliers can use the inspection directly to disclose or identify grievances and opportunities for improvement as well as to initiate appropriate measures.

Information and ideas from customers can, for example, lead to improvements in employee health protection. The exchange of experience with customers can also lead to joint projects, for example in the use of resources for products or logistics.

1. Self-declaration: What should your company pay attention to?

- **Answering the questionnaire:** Diligence and accuracy in filling out the self-declaration form create transparency and provide information about one's own competence. It also enables targeted action in the event of grievances.
- **Internal responsibility:** The training and education of a sustainability officer as the main person responsible and primary contact person for customers ensures the quality of your information in the self-declaration. Communication processes with the customer are facilitated.
- **Documentation:** Evidence of codes and certificates of management systems strengthen the credibility of your self-declaration. They provide the customer with important information about already existing guidelines, which play a role in the supplier evaluation, but also for the subsequent supplier development.

2. Audit: How should your company prepare?

- **Hotspot identification:** You should know risks in your business area and in your supply chain. Your information can be cross-checked with the auditor. This increases your credibility in the continuous improvement of your production or service processes.
- **Preparation of employees:** The sustainability officer (if any) should prepare your employees for the upcoming audit. Preparation includes explaining the audit process, the rights and obligations when interviewing employees, and possible consequences for the company.
- **Training of employees:** The training of employees and management personnel to follow set codes of conduct and standards should not take place shortly before auditing, but immediately upon introduction of management systems. Regular follow-up training ensures active integration into everyday business.

3. Next steps

- Familiarize yourself with the (new) sustainability criteria of your customers. Ask specifically whether requirements for suppliers have changed or will change as a result of the German Supply Chain Due Diligence Act.
- Look at the customer's (new) Code of Conduct or self-disclosure and check whether you can meet the sustainability issues and requirements listed therein (including prohibition of all forms of child and forced labour, compliance with essential occupational health and safety measures, compliance with environmental standards).
- Check which (certified) management systems and labels for environment, energy, occupational health and safety and sustainability you already use or could use, which are accepted by your customers as proof of a high level of sustainability.
- Ask whether customers rely on industry solutions or cross-industry supplier platforms for supplier screening and familiarize yourself with them. An overview of industry initiatives is provided by the website "[CSR Practice Days](#)" (in German only), which is sponsored by the Federal Ministry of Labour and Social Affairs. Examples of platforms are Achilles, Business Social Compliance Initiative (BSCI), EcoVadis, NQC and Sedex Global.
- If you receive a large number of different requests from companies (e.g. in the form of different self-disclosures or queries via different supplier platforms), it may be useful to work with the industry association or with your chamber of commerce to make customers aware that this poses challenges for your company (and possibly others).

Further information

- **Further information on supplier screening** is provided in the guides "[Sustainable supply chain management for medium-sized companies in the chemical industry](#)" (English version available) by Chemie³ and "[Process steps for sustainable supply chain management](#)" by econsense.
- **Industry benchmarks** can help to get a sense of sustainability requirements. The [World Benchmarking Alliance](#) provides a free and publicly available sustainability benchmark where companies are rated on their sustainability performance and contribution to the achievement of the Sustainable Development Goals (SDGs).
- **Company examples of** how to deal with suppliers can be found in the guide "[Sustainable supply chain management in practice](#)" (in German).
- The Federal Government's [Helpdesk on Business & Human Rights](#) can provide advice on how to organize supplier screening.