



## Risk-Based Supply Chain Auditing

Supply chain audits of your suppliers, factories and global operations are an essential component to safeguarding your brand. Compliance with social responsibility, sustainability, trade security, anti-bribery, health and safety, conflict minerals and product quality assurance (GMP/GDP) are challenges that all organizations face. The risks are endless, and they continue to expand as a consequence of globalization.

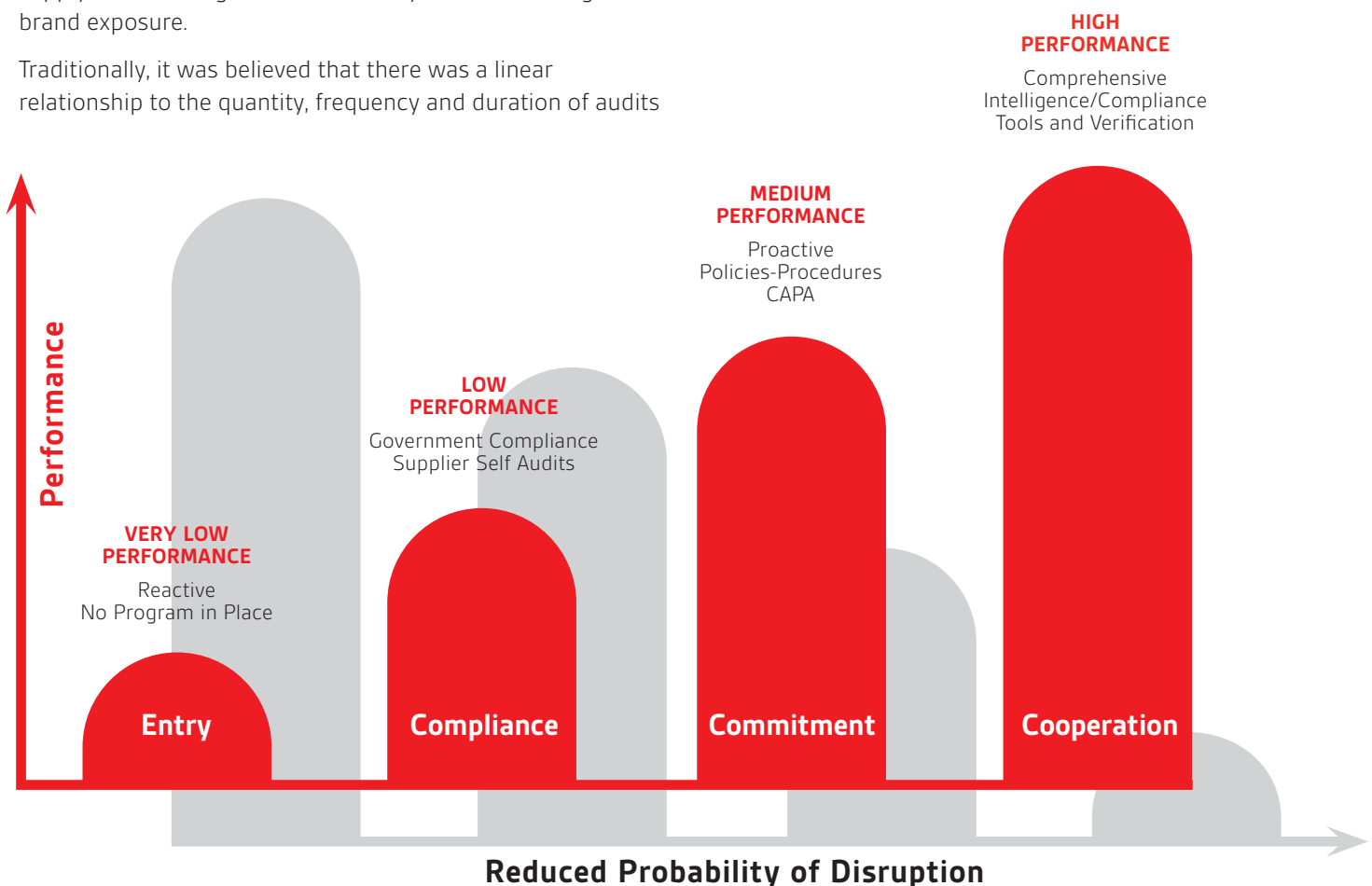
Proactive and progressive supply chains are outperforming traditional audit program methods by encompassing a wide range of audit criteria amassed over the years. Effective supplier verification programs require an intelligence based analysis of the people, processes and tools involved within the business landscape in which they operate. A good supplier auditing program is the backbone of driving business improvements by managing suppliers, which in return, reduces risk.

The first step is mapping out the direct and indirect suppliers in the supply chain. The more complex, diverse, and outsourced the supply chain, the greater the potential risk. It is not uncommon that organizations have difficulty identifying all of their suppliers. Consequently, it is mandatory that organizations institute controls and leverage supply chain intelligence to effectively tackle and mitigate brand exposure.

Traditionally, it was believed that there was a linear relationship to the quantity, frequency and duration of audits

to risk. Not only does this drive higher cost - and doesn't identify and target the highest risk suppliers upfront - it comes at a cost of continued supply chain exposure. A large supplier base will outpace the resources of a passive supplier audit program. It is critical to identify the highest risk suppliers to focus on upfront.

In addition, organizations may also face internal challenges - several divisions managing their own commodity and supplier base - in an uncoordinated fashion, and functioning with segregated data - thereby fostering redundancy, limiting transparency, and lacking a homogenous approach to tracking and managing suppliers. It is therefore critical that an organization take an effective approach to targeting high risk suppliers, and implementing the foundation and processes for consistent oversight.



Despite internal and external challenges, organizations are compelled to establish effective programs around labor and environmental practices, responsible and ethical sourcing, and efficiencies around energy, water and planning for a business disruption. The increased pressure on organizations requires of firms to execute a comprehensive supply chain strategy inclusive of the people, processes, and systems to deliver on the promise of a resilient supply chain. Embedding a sensible approach to supply chain operations that represents interests in corporate social responsibility, quality, sustainable environment, and responsible sourcing will yield returns in corporate performance and business excellence.

Across several industries, new bars are being set. The apparel industry, for example has adopted the Life Cycle Assessment (LCA) program to identify and measure the effect of all materials for clothing, such as fabrics, trims, and packaging impact on the environment. The cost of poor quality is well understood, and further underscored is tight supplier management - established through compliance audits - ensures transparency and provides a framework for ethical sourcing. Some industry giants, such as Nike have taken it a step further by implementing the Materials Sustainability

Index (MSI) for its supply chain team as a whole to access an open source database on materials from early product development stages.

There has never been a greater need for supply chain transparency. Understanding the ramifications of sourcing decisions, and tight scorecard management of the supplier base are necessary to defy risk in supply chain. Supplier verification audits are a conduit to reducing business disruption and driving performance by managing risk to develop resiliency in the supply chain.

A reactive organization that doesn't implement a supply chain risk management program is likely to face greater disruption and poor performance as the speed and agility to react will be much slower than the organization that implements all the supply chain levers - intelligence, compliance tools and supplier verification audits.

BSI is a proponent of using intelligent based risk analysis to understand, manage and confirm the business, financial, brand reputation risk to an organization. Leveraging tools and targeting supplier verification audits to high risk suppliers provides unparalleled insight into the supply chain.

## 1.0 Understanding Supply Chain Risk

BSI risk consultants work with organizations to understand and define the critical interdependencies of supply chain risks along the entire product journey. Identifying the highest risk areas enables an organization to manage, mitigate and plan effectively. Risks can be external - natural and man-made disasters, terrorism - or internal - responsible sourcing, corporate social responsibility, environmental, just to name a few examples. BSI tailors its consultancy services to help organizations understand where their risk lies, and implement a course of action that builds resiliency in the supply chain. Using our proprietary Supply Chain Risk Exposure Evaluation Network (SCREEN) intelligence platform, our consultants can determine which suppliers pose the greatest risk and high risk countries that the supply chain may experience disruption. This enables an organization to focus on the foremost risk areas likely to provide financial, brand or reputational damage. Unlike other audits in the market, BSI's supplier verification audits can include client specific areas for a more custom approach, and are led by auditors with years of industry and compliance expertise globally.

# The Audit Process

## 1.1 Supplier Self Assessment

A Supplier Self Assessment is an opportunity for your organization to have an informal preliminary audit that will help identify areas of weakness in your supply chain. Once the supplier completes a self-assessment, results are immediately available for review. The assessment report will identify major flaws or gaps for a supplier and provide focus on the greatest risk areas to address. A Supplier Self-Assessment is usually about half the length of a full audit and commonly takes place 60-90 days prior to the on-site evaluation.

## 1.2 Onsite Audit

A supplier verification audit will cover:

- Documented processes and procedures
- Corrective and Protective Actions (CAPA) inputs - issues, root cause, implementation and effectiveness check
- Risk assessment and prioritization
- Action plan, escalation and metrics to track progress of nonconformities

Key inputs into a supplier verification audit include:

- Records Review - Quality (GMP/GDP), CSR, Sustainability, Anti-Bribery, Conflict Minerals, BCM
- Process Management, Nonconformities
- Identification of hazards and risk
- Risk control decision points

The risk decision points can run the gamut - from supplier performance, environmental conditions, and controls in place around process and product quality, complaint handling, and so on. The bottom line is that the risk priority is assessed consistently across all suppliers. The supply chain audit team uses a best practice, standardized approach to audits - leveraging program tools, document management,

corrective and preventative action follow up, and supplier verification - to apply the same level of scrutiny to all suppliers.

Manufacturers look for assurances from their supplier base that they are adhering to the requirements that they set forward. These requirements can encompass:

- Quality Agreements (GMP/GDP) - providing quality assurance that products are produced and controlled consistently - and in the case of Pharmaceutical and Food, with no risk of cross contamination
- Conflict Minerals - responsible sourcing to end human rights violations
- Environmental Compliance - identify and manage the environmental impact of an organization's products, and ensure environmental performance
- CSR - Human Rights, H&S - ensuring socially responsible, fair treatment of employees, as it pertains to H&S, wages, underage workers, etc.
- Import Compliance/Trade Security - risk of unmanifested cargo, counterfeiting, theft
- Business Continuity - assurances that in the event of business disruption, a supplier has a plan in place to quickly/effectively resume business operations

The expectation from manufacturers is that the product or service meets their product specifications. Verification audits of supplier factories, quality system process controls are necessary activities for a supplier to remain in good standing. Typically, a quality agreement is in place outlining the requirements of a finished product. The product or component that is distributed must comply with federal, state and local environmental regulations. Due to any potential interruption encountered in the supply chain, it is prudent for an organization to expect of their suppliers a business continuity plan denoting a clear action plan, checklist of activities, communication plan, escalation measures, and team roles. Open communication lines between the supplier and manufacturer must be

## Supplier Controls

**Supply Chain Risks**  
Quality (GMP)  
Conflict Minerals  
CSR, H&S, BCM  
Anti Bribery

**Transport Risks**  
Distribution (GDP)  
Trade Security

**Location based Risks**  
Risk based Procurement  
Supplier Country &  
Risk Profiles

**Risk Reporting**  
Supplier Scorecard  
Business Reviews  
CAPA closure

demonstrated at all times. The expectation on the supplier is that the business protects and enforces CSR human rights, fair wages and labor standards. In Today's global market, a safe working environment is not an option, it's a must. The Dodd-Frank legislation places greater scrutiny on manufacturers to ensure their supply chain is conflict mineral free, which will continue to challenge suppliers to implement ethical sourcing and accurate tracing of material origin of source.

A supply chain verification audit will have the versatility to maximize every audit to additional areas an organization may be seeking information about - or troubling factors systemic of that region such as counterfeit risk, social and environmental risk, ethical sourcing, etc.

BSI approaches every audit with a three pronged risk assessment approach:

1. Determining the criticality of suppliers or strategic impact on the supply chain. This includes identification of high risk, low compliance suppliers and low risk, high compliance suppliers to determine where focus and resources need to be placed
2. Understanding supplier risk profiles and quantification of risk and compliance exposures
3. Assess the controls in place for suppliers. This additionally touches on program effectiveness - average time for corrective action closure, root cause analysis and action planning

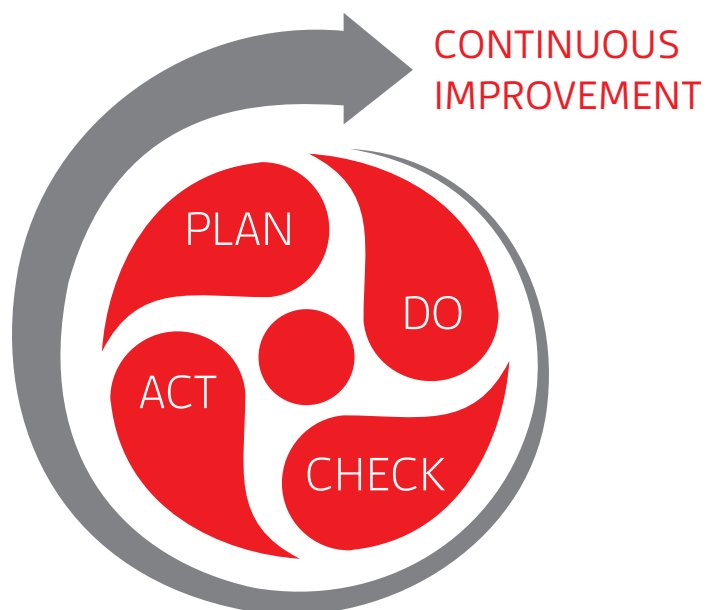
A supplier verification audit provides a bird's eye view of many aspects of a supply chain program. Transparency is real time and program data is uploaded into the BSI's Supplier Compliance Manager (SCM) system for analysis. Verification can provide simple information such as location details and validating the supplier to more extensive information around validating corrective action implementation, reviewing documents to ensure that the code of conduct is being adhered to - as it pertains to CSR, Sustainability, Anti-Bribery, Conflict Minerals, and GMP/GDP compliance.

Audit gaps include nonconformities and any other areas of concern that could be classified as a nonconformity or opportunity for improvement (OFI).

BSI will report back to the organization key findings, and the supplier will be expected to carefully consider the time needed to resolve all nonconformities and areas of concern identified.

Based on the risk exposure, gaps identified and any other measures an organization wants to track with its supplier base, the auditor will conduct a document review with the supplier. The audit is conducted to:

- Audit your supplier's documentation and inform of any gaps
- Evaluate location(s) and any site-specific conditions
- Review the supplier's status and understanding regarding requirements from the organization, with respect to the identification of key performance or significant aspects, processes, objectives and operation of the supplier
- Collect necessary information regarding the scope of the supplier's role including processes and compliance (e.g. quality, environmental, health and safety, associated risks etc.)
- Evaluate if the internal audits are being planned and performed, and that the level of implementation substantiates that they are in good standing
- Evidence of compliance
- Operations control of processes
- Effectiveness of internal auditing
- Management responsibility for policies; and
- Linkage between normative requirements - policy, performance objectives and targets and any applicable legal requirements, responsibilities, competence of personnel, operations, procedures, performance data and internal audit findings and conclusions



### 1.3 Opening and Closing Meetings

A formal opening meeting will take place at the beginning of each supplier verification audit. This meeting is to cover the scope of the audit, and the overall process and agenda of the audit. Similarly, a closing meeting will be held at the end of the audit to report the major findings that will be presented to both the supplier and the organization. A clear explanation will be provided about the process for closure of any nonconformities including timeframes and expectations about verification, review and acceptance.

### 1.4 Certificate of Excellence

Following a supplier verification audit and after review, acceptance, verification of the effectiveness of correction, root cause analysis and corrective actions for Major nonconformities and review and acceptance of your planned correction, root cause analysis and corrective action for Minor nonconformities, BSI will conduct an independent review. As evidence of compliance the supplier will be presented with a signed certificate. It normally takes 4 weeks to issue a Certificate of Excellence following formal acceptance of your corrective actions as described above in this paragraph.

### 1.5 Re-Verification Audit

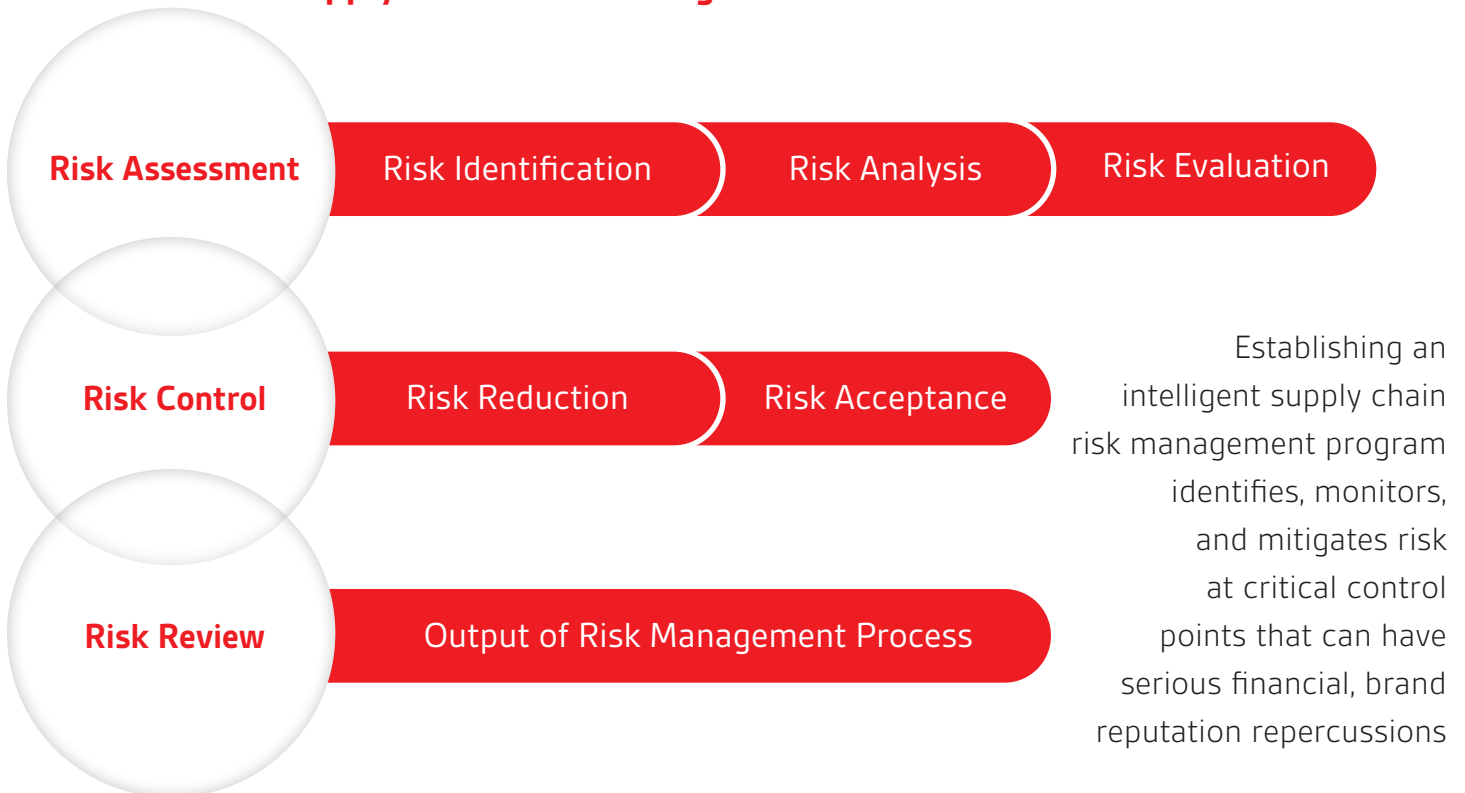
Annual supplier verification involves an on-site audit. The purpose is to:

- a) Verify overall continuing effectiveness of your compliance in its entirety in light of internal and external changes and its continued relevance and applicability to your scope
- b) Demonstrate the supplier's commitment to maintain the effectiveness and improvement of your processes in order to enhance overall performance; and
- c) Determine if the supplier's operation is achieving the organization's policy and objectives

### 1.6 Major Nonconformities

In the event that a major nonconformity is found during an audit, a special visit may be required at a later date to ensure this major nonconformity has been effectively closed down. Risk Communication

## Supply Chain Risk Management Process Framework



# BSI Global Training Capabilities

As the leading global Standards body, BSI has a long and rich history of developing many of the world's leading standards. As such, BSI Global Training Academy offers a large portfolio of training courses which provide a practical and participative learning experience to optimize knowledge retention.

Training courses are available for a large range of topics including GMP, Corporate Social Responsibility, Business Continuity, Environmental (Water, Energy), Supply Chain Security, HACCP, Food Hygiene, Anti-bribery, Occupational Health & Safety and Business Continuity Management as a few examples.

## Account and Program Management

BSI offers account management support for its SCM hosted, or managed system. BSI's Client Account Management team will manage the distribution of supplier invitations, administer surveys, help desk, on-site verifications, CAPA's administration, escalation and follow-up.

**On-Site Workshop** - To initiate implementation of SCM, BSI will host an on-site workshop to ensure that SCM meets the organization's business needs and specifications.

**Quarterly Business Reviews** - BSI conducts Quarterly Business Review meetings to discuss program progress. These may be held remotely, via teleconference, or on-site at the organization's location.

**Third Party Administration** - BSI provides managed services for your SCM account for an additional fee. BSI SCM Managed Services acts as an extension to your team which enables an organization to use BSI Supply Chain representatives as an interface with their global supplier base. Included in this service is all communications with your suppliers, corrective action planning with non-compliant suppliers and assessment refreshers.

**Program Management for Onsite Supplier Verification Services - BSI VerifEye™** - A Program Manager is assigned for large multi-country global accounts to ensure the BSI Verification program is set-up properly according to client requirements.

Program Management team is set up to deliver excellent customer service, timely and instant responses to our BSI clients and their suppliers, closely monitor the quality of the program, review existing working procedures and work out improvement plans. The names, titles, locations and responsibilities of these staff members will be provided to clients following acceptance of this proposal. Internally, all team members have close working relationships which ensure the most up-to-date requirements are cascaded to and adopted by relevant local teams.

Program Management functions include:

- Establish, review and maintain client specific program documents and communicate with BSI operations network to ensure services consistency
- All program procedure documents required to support operational alignment are updated to the BSI support group network
- Implement and monitor internal controls relating to client specific program KPI's
- Centralize point to handle customer global activities such as procedure updating, performance review, inquiries and complaints resolution
- Take necessary corrective & preventative action to improve execution & client service
- Work with customer to prepare, organize and deliver supplier, vendor related training as needed

# Why BSI – Global Footprint, Local Operation

Many supplier certification programs rely solely on supplier self-reporting to achieve and maintain compliance. BSI believes that a more stringent audit program is required to really know who your suppliers are and what they are doing in order to protect your brand, reputation and customers. BSI's on-site verification audits are conducted by in-country experts - fluent in local languages and customs - that conduct over 100,000 audits each year for thousands of companies. A proven approach, BSI will go on-site to the supplier location and conduct factory tours, employee interviews, documentation reviews, supply chain reviews and supplier risk profiles. These Supplier Verification Audits provide an efficient and comprehensive audit of suppliers. BSI Supplier verification audit reports are entered into the Supplier Compliance Manager tool to provide an in-depth overview of supplier compliance and risk. Our global supply chain risk intelligence is infused into each supplier audit report, providing complete visibility into suppliers' practices and potential risks. The objective is to deliver actionable data to ensure compliance and mitigate risks within your supplier base.

The gold standard for a supplier verification program is a versatile, nimble multi module system that pools together the process, resources, tools to deliver transparency across the supply chain providing an actionable, progressive program in lieu of a static, passive program.

The supplier chain audit program requires a seasoned operational structure capable of implementing best practices, and bringing together the process, intelligent data sets, supply chain tools, to drive a standardized approach across the supplier base. Implementation of audit protocols is critical to bring a comprehensive approach; it does not suffice to simply do a cursory inspection and checklist to derive the analysis and results that are needed to make good business decisions. In addition, auditors need to be locally based, be familiar with local laws and culturally adept at what to look for.



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