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OECD Due Diligence Guidance Downstream Progress Report Detailed Findings

OECD
Multi-Stakeholder
Forum
May 3, 2012

Goals of session

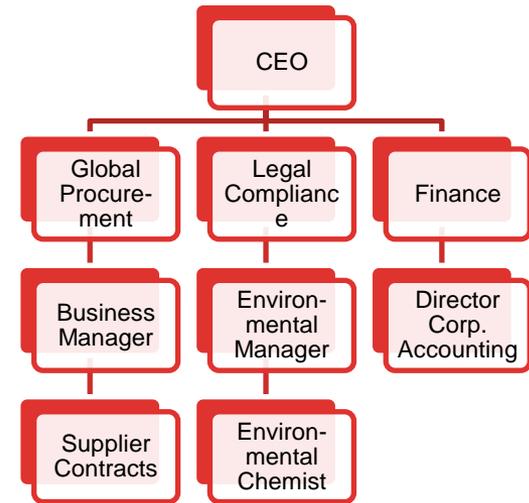
- Provide detailed findings on the downstream progress report according to the five-step OECD Framework
- Answer clarifying questions
- Generate a constructive discussion among all stakeholders
- Identify 3-4 topics for deeper discussion during break-out session on Day 2
 - These topics should align with the issues that are reported back to the afternoon plenary session
 - Volunteers will report back to the plenary following the break out session

Step 1: Establish strong company management systems

Team and policy (Step 1A-B)

Team

- Most common practice employed is the assembly of cross-functional teams from a range of the following departments: engineering, legal, public relations, quality, supply management, and corporate responsibility.
- Others have dedicated one full resource to the issue



Policy

- Majority of participants have a policy in place
- They outline company commitment, due diligence activities, and supplier requirements.
- Many policies integrated into supplier code of conduct
- Efforts to align with Annex II of the Guidance

“... We prohibit human rights abuses associated with the extraction, transport or trade of minerals. We also prohibit any direct or indirect support to non-state armed groups or security forces that illegally control or tax mine sites, transport routes, trade points, or any upstream actors in the supply chain. Similarly, [company name] has a no tolerance policy with respect to corruption, money-laundering and bribery. We require the parties in our supply chain to agree to follow the same principles.”—Pilot participant policy

Policy cont...

Example

1. Drafted policy by extracting a prior statement on the issue, supplier code of conduct, and the OECD Guidance from three sources;
2. Reviewed Annex II to identify what was relevant for downstream companies (paragraphs 1–4) and what sections are modeled for upstream actors (paragraphs 5–14), in particular regarding some aspects related to the implementation of recommended risk-management strategies and applicable upstream only;
3. Reviewed the draft policy with a cross-functional team for review; and
4. Published the policy online

Challenges

- Ensuring that the policy does not promise results that companies are unable to uphold, and coping with the challenges and expectations around supply chain transparency
- Managing expectations for controlling the behaviour of upstream actors where there is no direct relationship
- Grappling with uncertainty around the final implementation of the SEC rules on Section 1502 of the Dodd-Frank Act
- Drafting a concise policy that allows them to communicate the lengthy, complex recommended policy efficiently to suppliers who may have limited resources and/or language barriers

Data collection and management (Step 1-C)

Data collection methods

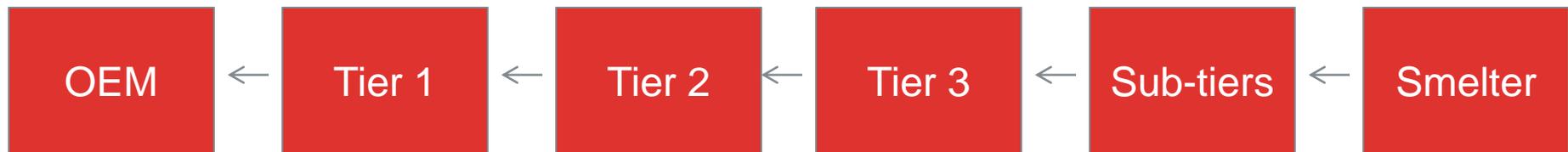
- Most commonly used tool is the EICC & GeSI Reporting Template
- AIAG web-based tool to track the smelters used
- IMDS (International Material Data System) to track material content
- Other companies are combining the EICC & GeSI Reporting Template with internal processes
- On hold for Dodd-Frank

Example of Hybrid Approach

One company is in the process of creating an integrated IT system to manage and gather data, communicate with suppliers, and generate metrics and reports.

1. Using existing systems used for compliance with REACH using a supplier survey developed internally
2. Using a 'social network' tool where suppliers can self-register to gather information on their own supply base

Information collection process



Data collection and management challenges

Companies face a number of challenges related to data collection and management.

- Incompatibility of the EICC & GeSI Dashboard with internal systems
- Creating a data collection system prior to the SEC's final rules may require the companies to later change their system, with implications for functionality, resources, and clarity
- The current EICC & GeSI template is used to collect information at the supplier level, but certain customers request information at the part level. The EICC & GeSI template does not allow for this level of detail. A revision of the EICC & GeSI template will include part-level capability

Supplier engagement (Step 1-D)

Methods

- Policy and contract clauses
- Purchase orders
- Letters from company executives
- “Dear Supplier” letters through industry associations
- Webinars
- Face-to-face information sessions
- Supplier meetings
- 1:1 phone conversations

In practice

- Send an initial awareness letter with general information on Dodd-Frank and the DRC conflict
- Second letter with specific expectations on submitting due diligence information
- Information sessions at supplier symposia

“...The following summarizes [company]’s minimum expectations for your response:

- Suppliers are to send this same request to their direct suppliers (using the same Reporting Template).*
- Suppliers are to disclose to [company name] the names of smelters used in their supply chain for tin, tantalum, tungsten and gold (by using the MRPRO software to create a rollup of smelter names provided by your suppliers)*
- Suppliers are to adopt their own conflict minerals policy (see [company name]’s updated Supply Chain Social and Environmental Responsibility Policy (weblink)...”—Pilot participant supplier letter*

Customer communications (Step 1-D)

Participants are also responding to customer requests on 3T&G due diligence

Types of data requests

- Surveys on the use of 3T&G
- Smelter/mine name and existence of a policy
- Initiatives for non-use
- A signed memorandum on the non-use of conflict-affected 3T&G
- Provision of a non-use certificate

Content of communications

- Surveys on the use of 3T&G
- Details on company's approach to due diligence (i.e., while regulation is not final, efforts are still being made to trace minerals in the supply chain)
- How 3T&G is used and in which product categories
- Where the company currently stands in rolling out its due diligence (i.e., whether products have been identified, or companies are awaiting feedback from requests they have sent suppliers)
- Method for obtaining information (e.g., EICC & GeSI reporting template)
- Estimate of when the information will become available
- Participation in industry collaboration and other engagement activities

Step 1: Discussion Questions

Key questions

- *What has been a key learning in implementing or making progress on this step?*
- *What do you foresee as the biggest challenges to make progress on this step?*
- *What support from the international community can help advance progress?*

Step 2: Identify and assess risk in the supply chain

Supplier identification (Step 2-A)

Findings

- Most participants have begun or have already identified Tier 1 suppliers and/or products containing 3T&G
- Several participants have received information Tiers 1, 2 and 3
- Three respondents are not identifying suppliers until the final SEC ruling

Approach 1: Identify commodities that do contain 3T&G (and consequently reach out to those related suppliers).

1. Search through procurement data for all products containing 3T&G
2. Identify information from material declaration system to identify the suppliers of those chemicals, materials, and components
3. Conduct targeted supply chain surveys using the information obtained through the Procurement system.

Approach 2: Eliminate commodities that do not contain 3T&G

1. One company analysed 200+ commodity groupings to prioritize those that contain 3T&G and those that do not
2. Worked with manufacturing sites to determine a list of suppliers
3. Consolidated all suppliers based on the analysis to prioritize approximately 1% to send due diligence requests

Supplier prioritization (Step 2-A)

Trends

- Prioritize sub-set of Tier 1 suppliers
- Communicate with all Tier 1 suppliers
- Communicate with Tier 1, 2 and 3 suppliers
- Communicate with all suppliers (regardless of tier)

Risk assessment methodologies

- Percentage of 3T&G content in the product
- Spending or percentage of annual purchases from the supplier
- Position of the supplier on the supply chain
- Relevant commodities and product types
- History and strategic importance of the supplier

In practice

One company prioritized 350 suppliers with the following criteria:

- Spending as the priority suppliers represent 75 percent of purchasing volume
- Proximity to the smelter since those that are closer have a higher likelihood of executing reliable supply chain investigations
- Relevant commodities
- Quantity of 3T&G in supplier products

Validating supplier responses

Majority of participants are validating responses manually

Basic criteria

- Ensure that suppliers complete all mandatory fields
- Conform that they have a policy and process in place
- Check to ensure that responses include smelter names

Common sense methods

- Percentage of 3T&G content in the product
- Review the material content of parts bought from suppliers to validate the absence or presence of 3T&G.
- Conduct Internet research on all smelter names provided for validity and require corrections to any that are invalid.
- Ensure that the number of reported smelters matches up with the size of the supplier.
- Check whether the supplier lists at least one smelter for each of the metals where they indicate that they identified all the smelters.
- Confirm that the smelter names provided are actual smelters.
- Check the smelter addresses to identify any inconsistencies.
- Compare the smelters provided by suppliers to the published CFS smelter list.

Identifying smelters (Step 2-A)

The majority of participants are still working to identify smelters through industry processes unless they have direct relationships

- Most participants are relying on the CFS program to engage with smelters and verify their due diligence practices
- Industry associations are sending smelter 'encouragement' letters and providing a template for individual company letters to engage with smelters and request that they provide data on country of origin
- Companies are providing a list of smelters that have already been identified through the CFS program to ease the burden on suppliers
- Companies are contractually obligating suppliers to provide a certain level of disclosure as a precondition for doing business
- Reevaluating business awards based on suppliers' non-compliance with requirements
- Escalate supplier refusals to company management
- Using non-disclosure agreements to overcome confidentiality issues

Identifying smelter challenges

Companies face a number of challenges related to identifying smelters

- Developing NDAs is time-consuming.
- Overcoming confidentiality concerns of suppliers' suppliers where there is no contractual relationship.
- Anti-trust issues prevent companies from dictating that suppliers source from verifiable conflict-free smelters.
- Information technology systems will not help to overcome the issue of disclosure with smelter names in cases where suppliers push back about confidentiality of smelter names, not just supplier information.
- Because manufacturers do not have a legal right to unilaterally revise contract terms during the duration of a contract, they can only include specific terms concerning conflict minerals in contracts as they are signed or renewed. Consequently, it may take a company three to seven years to include such clauses in all of its contracts, depending on the duration of its existing contracts.

Obtaining data and information from smelters

Eleven companies intend to collect smelter information through the CFS program

Data requests

- Identification of smelters used
- Statement on mine and country of origin
- Sourcing policy on minerals from conflict-affected areas
- Declaration of compliance status
- Explanation of suppliers' management system
- Confirmation that suppliers understand companies' expectations
- Accurate material content reporting over 12 months
- Conflict-free materials, components, and parts

Step 2: Discussion Questions

Key questions

- *What has been a key learning in implementing or making progress on this step?*
- *What do you foresee as the biggest challenges to make progress on this step?*
- *What support from the international community can help advance progress?*

Step 3: Design and implement a strategy to respond to identified risks

Risk management

The majority of participants are still in the early phases of developing a risk management approach. Common components that emerged include:

- **Supplier communications and trainings:**

Participants are communicating and reinforcing corporate policies during key supplier meetings

- **Setting clear requirements through policies and contractual clauses:**

Participants are enforcing compliance to their policies by requiring supplier declarations, the incorporation of contract clauses, and terms and conditions flow downs on minerals from conflict-affected areas.

- **Internal review processes with non-responsive or noncompliant suppliers with upper management**

*“SECTION 26. TERMINATION FOR CAUSE
26.01 Supplier Breach The Buyer may terminate a Purchase Order, in whole or in part, upon Written Notice to the Supplier if the Supplier fails to comply with any of the requirements of the Purchase Order. If the noncompliance relates to an obligation of the Supplier that is, in the opinion of the Buyer, capable of cure as described in Section 26.02, the Buyer may terminate under this Section 26.01 only if the Supplier has failed to either: (a) timely cure the noncompliance (as described in Section 26.02); or (b) provide the Buyer with adequate assurances of performance acceptable to the Buyer.”—Pilot participant termination clause*

Risk mitigation

Because the majority of participants do not have direct relationships with smelters, they indicated that they are not mitigating risks on their own.

- Companies are relying on the CFS Program to mitigate risks (smelter and beyond), citing industry-wide collaboration as the only way to properly address supply chain risks.
- Companies that have risk mitigation processes in place have indicated the following actions when a supplier is in violation of company policy:
 - They take immediate action to make improvements and require the supplier to take corrective action
 - Continued non-conformance and refusal to address issues of concern will lead them to terminate the business relationship

Step 3: Discussion Questions

Key questions

- *What has been a key learning in implementing or making progress on this step?*
- *What do you foresee as the biggest challenges to make progress on this step?*
- *What support from the international community can help advance progress?*

Step 4: Carry out third-party
audit of smelters/refiners' due
diligence practices

Conducting audits

Participants with direct smelter relationships

- One of four companies with direct smelter relationships conducts its own audits on 3T&G due diligence
- The remaining three companies rely on industry processes to conduct audits
 - EICC & GeSI CFS Program
 - iTSCI
 - ATTA (the American Tin Trade Association)

Participants with only indirect smelter relationships

- Companies without direct smelter relationships are unable to request, obtain permission, or perform audits
- 13 companies are participating in the CFS program by
 - Joining smelter visits
 - Acting on the Audit Review Committee
 - Providing financial support
 - Assisting in the enrollment of smelters

Smelter audit challenges

Companies described the following challenges related to auditing smelters

- While the CFS has published a list of 11 conflict-free tantalum smelters, tin and tungsten smelter lists are unavailable for all smelters conflict-free or not.
- Because of anti-trust requirements, CFS does not provide information about which smelters are in the process of becoming CFS listed or which smelters are undergoing a continuous improvement plan. CFS does not report on who has not passed.
- Bottleneck around getting more smelters onto the CFS list because there are three auditors and only the CFS Audit Review Committee can certify a smelter.
- Lack of clarity around the process for auditor selection. (CFS has published on their website the due diligence process to increase transparency and ensure credibility and legitimacy.)
- Only one company expressed uncertainty as to whether “the CFS Program is the right tool to address the requirements of both Dodd-Frank and the OECD Guidance.”

Step 4: Discussion Questions

Key question

- *What has been a key learning in implementing or making progress on this step?*
- *What do you foresee as the biggest challenges to make progress on this step?*
- *What support from the international community can help advance progress?*

Step 5: Report annually on supply chain due diligence

Public reporting

More than half of the participants have started communicating publicly about their due diligence activities, while eleven stated they are waiting for Dodd-Frank

- **Proactive communication** via corporate responsibility websites, reports, blogs, and newsletters with the publication of corporate policies and codes of conduct and a description of their approach, activities, and recent developments
- **Currently externally communicating** policies on conflict-free sourcing, activities to identify smelters and mitigate risk, grievance channels, management systems, risk-assessment procedures
- **Plans for future reporting include:**
 - Reporting on the success rate of due diligence efforts with suppliers
 - Reporting efforts in the OECD Guidance implementation project
 - Quantitative results of due diligence process
 - Disclosure of smelter names in the supply chain

Step 5: Discussion Questions

Key question

- *What has been a key learning in implementing or making progress on this step?*
- *What do you foresee as the biggest challenges to make progress on this step?*
- *What support from the international community can help advance progress?*

The Role of Industry Associations

Industry associations: Information, resources, and education

All three industry association participants are supporting their members and industries on the issue

- **Formation of working groups:** two participants have formed working groups to provide information, facilitate industry and stakeholder engagement, form alliance and provide technical advocacy
- **Tools and instruments:** Associations are leading the development of systems and processes to obtain due diligence information and manage data.
 - The CFS Program is the only industry initiative in place to validate third party audits of smelters.
- **Member information:** Associations are providing general information and education opportunities for members more broadly outside of working groups through webinars, training sessions, FAQs, etc.
- **Smelter encouragement letters:** Industry associations are sending smelter 'encouragement' letters and providing a template for individual company letters to engage with smelters and request that they provide data on country of origin
- **Non-member benefits:** Associations are inviting non-members to participate in meetings and conferences, sharing available tools, and engaging with a broad range of stakeholders including NGOs, governments, and other industry sectors
- **Education on OECD Guidance:** All participants support their membership to better understand the Guidance through publications, web communications, event presentations, releases, direct mail and/or conferences.

Common and shared approaches

Data management tools

- **Data collection:** building tools for common questionnaires and data collection in order to facilitate consistency through the industry supply chain
 - **Confidentiality:** evaluating web-based solutions that can be used for data collection and roll-up within their industries that do not require listing all suppliers used within a company's supply chain
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Challenges of developing tools to meet requirements of both OECD and Dodd-Frank:

- Roll-up functionality
- Part level tracking
- Definition of a standard reporting requirement that meets the needs of all participants
- Lack of smelter/refiner participation because of audit costs

Smelter identification and verification: CFS Program

EICC & GeSI CFS Program is the only industry initiative in place to validate third party audits of smelters.

The CFS program:

- Addresses the needs of both the OECD and future Dodd-Frank requirements.
 - Works through member companies to gather smelter data via the information members receive through the CFS reporting template.
 - Has developed a list of 150 identified smelters
 - Initial focus is on tin and tantalum, and work has begun with tungsten and gold
 - Completed 16 tantalum smelter audits, with 11 verified as compliant
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Process

- Consolidate a confidential list of smelter information
- Identify real, known smelters and eliminate name variances and identifies entities that are not smelters or require more evaluation
- Companies use aggregated smelter information to improve their own lists

Smelter lists that companies have been able to collect represent approximately a

30:1 ratio

of invalid names to valid smelters.

Industry Associations: Discussion Questions

Key question

- *What has been a key learning about Industry Associations participation in the pilot and implementation of the OECD Due Diligence Guidance?*
- *What do you foresee as the biggest challenges for industry associations?*
- *What support from the international community can help advance and support industry associations?*

Downstream break-out topics

Break-out process and themes

Participants should identify and agree on 2-4 themes for discussion during the second break-out session for deeper discussion

Goals of break-out session:

- Participants will engage in a facilitated discussion on 2-4 issues identified after the first break-out session
- For each topic, participants will explore ways to overcome identified challenges
- Volunteers will report back to the plenary session on each topic

Potential themes:

- Data management and collection
- Prioritizing suppliers for risk assessments
- Validating data
- Overcoming confidentiality challenges
- Reliable smelter identification systems
- Is a conflict minerals declaration system in development? What would/is needed to have this?
- If and how can institutionalized mechanism can support existing industry initiatives
- Process for advising the two OECD DDG Supplements in light of the pilot implementation experience.

Thank you