The Social Compliance Industry’s “Inconvenient Truth”

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Background

- Social compliance efforts started in the early 1990s in response to negative media attention and campaigns;
- For the last 15 years, efforts have mostly focused on:
  - Developing a code to address minimum;
  - Basic training on the code and local legal requirements;
  - Performing audits against these standards; and
  - Demanding corrective action for those who fell short on compliance.
- Most factories in China have been forced to make cosmetic adjustments to their operations, hiding their normal business practices, as well as other efforts to pass audits;
- Audit industry lacks oversight, consistency, and professionalization;
- Simultaneously, retail and first cost prices have reduced considerably while material, labor and other costs have increased;
- Factories better able to “game” the system end up getting passing grades and therefore more business – we are rewarding the wrong factories.
Typical Factory – China

• Work between 70 and 100 hours per week;

• Pay between 800-1500RMB per month;

• 20-40% of workers do not get paid local minimum wage;

• 50-90% of workers do not get paid proper overtime wage (1.5, 2.0);

• Typical wage gap between actual vs. legal is between 150-500RMB per worker per month.
Falsified Records

Mexico: 5%
Bangladesh: 17%
China: 68%
Falsified Records in China: Reasons

- Long working hours (up to 100 hrs per week);
- Strict China laws (max 49 hours per week);
- Rigid Code requirements (max 49 or 60 hours);
- Variance in buyer requirements (60 vs. 72);
- Compensation based on piece not time;
- Significant minimum wage and overtime pay deficiencies (big pay gaps);
- Variance in legal interpretations (compensation for public holiday, overtime based on piece rate average);
- Variance in emphasis (focus on some issues but not others).
Social Compliance Implementation:

5 Company Types

**Free Rider:**
- No code
- No audits

**Pirates:**
- Have code
- Perform superficial audit using QC staff
- No training
- No capacity building
- No remediation
- Believe model is working

**Children of Light:**
- Have code
- Perform audits
- Uncover many violations
- Beginning to see patterns that show improvements are minimal
- Unwilling to relax their standards because of perceived PR risk

**Pragmatists:**
- Recognize the limitations of the model
- Willing to relax standards
- Pursuing capacity building and continuous improvement

**Revolutionaries:**
- Transform buying practices
- Pay for compliance
- Strategic partners
- Shared sacrifices

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*infact Responsible Manufacturing Solutions*
Social Compliance Implementation: 5 Company Types

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- Majority of companies with social compliance programs;
- Efforts are at a cross-roads;
- Driving key issues underground;
- Need to make substantial adjustments to their program and business model;
- Otherwise, they are being complicit and rewarding factories better able to game the system.
How can we stop this?
## Two Possible Ways

<table>
<thead>
<tr>
<th>Pragmatists:</th>
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Social Compliance Implementation: 5 Company Types

**Pragmatists:**
- Recognize the limitations of the model
- Willing to relax standards
- Pursuing capacity building and continuous improvement

- More and more companies moving in this direction (especially in China);
- Experimenting with different ways of encouraging transparency and continuous improvement;
- Performing more root-cause analysis;
- Pushing for incremental improvement;
- Still have not linked performance with business.
Continuous Improvement Progress

- Falsified Records: 68%
- Wage & Benefits: 95%
- Working Hours: 81%
- Record Keeping: 46%
- Record Keeping: 24%
**Continuous Improvement Progress to Date***

<table>
<thead>
<tr>
<th></th>
<th>Average Minimum Wage Per Month</th>
<th>Average Working Hours Per Month</th>
<th>Total Legal Wage Per Month (including overtime)</th>
<th>Average Low Wage Per Month (bottom 20%)</th>
<th>Average Wage Per Month</th>
<th>Average High Wage Per Month (top 20%)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>First Month</strong></td>
<td>$63.60</td>
<td>328.5</td>
<td>$187.25</td>
<td>$78.84</td>
<td>$124.83</td>
<td>$193.82</td>
</tr>
<tr>
<td><strong>Current Month</strong></td>
<td>$66.94</td>
<td>333</td>
<td>$199.80</td>
<td>$93.24</td>
<td>$139.86</td>
<td>$243.09</td>
</tr>
<tr>
<td><strong>Average Increase</strong></td>
<td>5%</td>
<td>1%</td>
<td>7%</td>
<td>18%</td>
<td>12%</td>
<td>25%</td>
</tr>
</tbody>
</table>

* First month versus current month will vary by factory since participants entered the program at different intervals.
Social Compliance Implementation: 5 Company Types

**Revolutionaries:**
- Transform buying practices
- Pay for compliance
- Strategic partners
- Shared sacrifices

- Rare (handful of companies or within core businesses);
- Have long-term relationships;
- Majority of production/capacity;
- Partner on real solutions;
- Willing to pay for performance.
Suggestions: Brands/Retailers

To truly impact compliance levels on the ground,

• Consider shifting from a model of compliance to a model of continuous improvement;
• New model would require less auditing and more education and capacity building;
• New model would also require longer term corrective action plans based on incremental improvement (not overnight compliance);
• Most importantly…..do more work internally to ensure that your sourcing department and social compliance can become more aligned.
Thank you

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