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# ESG Compliance Requires Supply Chain Scorecard Best Practice

## ESG:

- **E** Enviroment
- **S** Social
- **G** Governance

### There is real money associated with ESG compliance.

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| 2021 wildfires in the United States caused $90bn worth of damages. [1]– Environmental. | Boohoo: UK fast fashion brand lost over £1.5bn in two days due to poor working conditions in one of their Leicester factories. [2]– Social. | Government regulations on carbon could cost companies such as ExxonMobil $11bn annual in penalties, based on their 2020 emissions. [3]– Governance. |

**ESG has evolved in importance and moved beyond a messaging and "feel good" exercise** and evolved into a business requirement. There are real dollar values associated with ESG compliance. What started as an early movement around improved corporate governance, followed by a small but vocal interested community, has morphed into Government-mandated regulations that companies need to comply with and invest significant resources in to insure against reputational risk and lack of access to capital. Companies across a swath of industries are now realizing that signi ficant investment and sophistication is required in corporate approaches to ESG compliance. Whether it is due to consumers voting with their wallets or government regulations and penalties, ignoring ESG compliance has impactful financial and brand consequences.

## What is ESG?

**Simply stated, ESG stands for, environment, social and governance.** Three pillars to determine the impact your business has on the globe. Are you a good steward of our planet? Industries, companies, individuals, and markets are increasingly measuring the viability and worthiness of companies based on these variables. Each entity needs to measure which of these three is most relevant to their core business, which variable can have the greatest impact on your reputation and business viability.



[1] *https://www.accuweather.com/en/severe-weather/2021-wildfire-season-economic-damages-estimate-70-billion-to-90-billion/1024414?*
[2] *https://www.theguardian.com/business/2020/jul/07/boohoo-shares-concern-factory-conditions?*
[3] *https://hbr.org/2021/10/carbon-might-be-your-companys-biggestW-financial-liability*


Understanding which drivers impact your ESG efforts is complicated enough, but when we start looking at your supply chain, that complexity increases. Let's unpack the underlying reasons.

## WHY YOUR SUPPLY CHAIN CREATES ESG HEADACHES

**Supply chains have garnered a large amount of attention over the past few years,** in large part because of the negative impact COVID had all along our supply chains. From not being able to secure the proper PPE, computer chip shortages, not enough lumber for home builds, rationing of toilet paper in grocery stores, the list goes on. [4] The reality for supply chain professionalws  is that they are constantly dealing with disruptions. The pandemic brought these challenges to the surface for all to see. But what does this have to do with ESG compliance? Supply chains are the foundation of any business, but they are not linear "chains." They are truly networks. Let's look at how supply chains have evolved.

**When the term supply chain was first introduced** – on June 4, 1982, by Keith Oliver in an interview with Arnold Kransforff in the Financial Times [5] – the notion of a chain implied a linear process. From sourcing to the end customer, there was a logical progression from step to step until final consumption – a chain. However, the reality is supply chains are complicated networks. Comprised of layers upon layers of suppliers, manufacturers, transportation, storage, customer facing and sourcing nodes.

**Today, companies across all industries,** have hundreds at times thousands of separate entities that make their supply chain. The networks that supply chains are built on are complicated, intertwined and constantly evolving Supply chains are also rarely contained within one homogenous geography. They tend to stretch across national boundaries, time zones, cultural demographics and at times might cross back and forth over the same regions. Truly an intertwined network, not a linear chain.

**Take for example a simple product such as margarine.** Highlighted by Daniel Stanton in his book: Supply Chain Management for Dummies. Before it arrives at your local grocery store it starts at a vegetable farm. Those vegetables are harvested and transported to a processing plant, to turn that sourced material into vegetable oil. Those oils are then turned into margarine, potentially at another plant. Once the margarine is created it must be segmented and



[4] *https://www.whitehouse.gov/cea/written-materials/2021/06/17/why-the-pandemic-has-disrupted-supply-chains/*
[5] *https://supplychaindigital.com/digital-supply-chain/keith-oliver-the-man-who-gave-us-supply-chain-management*

placed into containers. That transport will be done in temperature-controlled trucks, to then be stored in a temperature-controlled warehouse. There the distribution center (DC) will store the pallets and break the containers into smaller pallets to be sent to the various stores and restaurants that the DC is supplying – leaning on other transportation nodes. [6] For a simple tub of margarine, there are multiple touch points – growing the raw material, creating the final product, moving the product, storing the product, and finally selling the product. Now imagine this as a more complex product – semiconductors, automobiles, pharmaceuticals, or electronics for example. The modern supply chains resemble a Gordian Knot. [7] And simply chopping it in half to untangle the knot is not a viable option. This very complexity creates challenges in addressing and meeting ESG compliance around ethical supply, forced labor, and anti-corruption measures. The large number of nodes that comprise the supply chain, the various geographies and physical distances, and myriad suppliers, make your network opaque and the requirement to invest in third party data for verification at every step of the supply chain critical. The value of this external data, empowers companies to get closer to a true representation of their supply chain. Too often supply chains, and their ESG compliance is too reliant on a high percentage of internal data, not painting a true picture.

How can these strains impact the different departments in your organization?

## WHO THIS IMPACTS

- **CPO (Chief Procurement Officer)** –
  Procurement departments must focus on how they can ensure where they are sourcing material. Factors such as whether materials being sourced are sustainable, are the working conditions at suppliers meeting with local social & legal requirements and what are potential impacts from regulations? This requires multiple data sources, most of which are outside a company's four walls. Monitoring working conditions through unstructured data, empowers the CPO to monitor potential working condition violations. Leveraging data that sheds light into where material is being sourced, coupled with government regulation data, ensures procurement can remain compliant.

- **CFO (Chief Financial Officer)** –
  The CFO and their department are always focused on the bottom line. With regards to ESG compliance there is the potential of severe financial ramifications when it comes to being ignorant of government regulations and legislation. Financial departments must ensure having a clear view on what this landscape looks like and what exposure there might be with their supply chain. Finance needs to have a clear, and up to date picture of all the possible regulations, penalties and fines - ranging from local municipalities to national governments. This requires a pipeline of regulation data to be monitored and most importantly married with actions within the supply chain related to these regulations.

- **CIO (Chief Information Officer)** –
  Increasingly, the office of the CIO is being asked to leverage data and technology in support of ESG goals. The



[6] *https://www.dummies.com/article/business-careers-money/business/operations/supply-chain-management-dummies-cheat-sheet-246398/*
[7] *https://www.forbes.com/sites/forbescommunicationscouncil/2020/06/08/tangled-why-global-supply-chains-are-so-complex/?sh=588126645bf5*

challenge for the CIO is how to best harness all the information from within the organization as well as how to leverage their IT to better collaborate across the supply chain with all the different actors and their data stacks. While the CIOs office is already tasked with ensuring clean and actionable data, they will be asked to ensure the proper systems in place to ingest a greater amount of external data. For ESG compliance, the CIO's office will have to ensure the proper technology, partners and mentality to ingest and leverage these data sources.

- **CMO (Chief Marketing Officer)** –
  Marketing departments are usually the furthest from supply chains, but when it comes to following ESG, marketing has much invested. One of the ramifications of poor ESG compliance is suffering from brand damage. CMOs must be on alert for any issue within the supply chain that could adversely impact the brand image of the company. While they might not have direct control over the supply chain activities, they are the ones that will have to deal with any brand repercussions. One focus for the CMO's office, leaning on external data to monitor sentiment to anticipate potential brand damage due to ESG shortcomings. How can marketers leverage external data, structured or unstructured, to identify events within the supply chain that will impact their business? CMOs can look to establish listening posts pulling in multiple forms of data to protect themselves from potential ESG pitfalls.

- **CSCO (Chief Supply Chain Officer)** –
  When it comes to ESG impacts and the supply chain, the head of the supply chain is of course the most concerned and potentially impacted. As we see more CSCOs at the c-suite, one of the main responsibilities falling on their plate will be ensuring ESG compliance is met. They will need to constantly strive to have a complete and real time view of their supply chain. From sourcing to the final customer. The CSCO requires a rich level of data to paint the true picture of the network. For example - are their regulations for importing into specific geographies that will impact strategy. Or are their specific manufacturing regulations that can have deep repercussions on the supply chain? The CSCO requires external data to better manage this, otherwise they will be continually reacting as opposed to being proactive with their supply chain. Focusing on how to best manage the supply chain to keep in line with the ESG goals set out by the business.

## WHAT YOU CAN DO

The core of your ESG compliance challenge is complexity – specifically from your supply chain, the network you rely upon to deliver your product or offer services to your customers.

- **Map your ESG compliance to your supply chain network**:
  Clearly identify and prioritize your ESG compliance goals. Each business will have different priorities when it comes to ESG. Once you have identified these goals, the key is to understand how your supply chain will have an impact on these goals. For example, if you source and much of your supply chain is international, being hyper

aware of governance issues is your priority. How will you ensure you have a clear view into the changing regulations? This will be your area of focus. Maybe your business outsources the majority of your manufacturing. The social aspect of ESG could be the priority as you look toensure all of your outsourced nodes are practicing a high standard of social oversight.

- **Ensure clean data – both internally and externally.** A hurdle that all supply chain professionals struggle with, is how to gain greater visibility across the network? Add to this the need to create ESG scoring matrixes, and the thirst for data only grows. For companies to better meet their ESG compliance goals, start with internal data. Understand what is happening within the four walls of your organization. But this can only get you so far. The majority of events that will impact your ESG goals are within your extended supply chain. Companies, and their supply chains, will need to find a way to tap into and leverage data from a multitude of sources, including special ist ESG data providers and data sets. Only with this type of data, married to your internal data, can supply chains truly manage their ESG compliance.

- **Clearly communicate to your organization and supply chain what you expect**. Finally to ensure you can meet your ESG goals, it will take the entire supply chain network to understand what are the goals and how to measure success and progress. Having open communication, and honest communication within the network is crucial. Companies need to ensure that this communication is also done on a regular basis, and this communication needs to be supported by data. Companies must ensure that they not only communicate but work with the key nodes within their supply chain to make the goals and measurements clear. The ability to paint a more complete picture, creates the proper environment for true understanding and agreement on ESG compliance direction. Depending on the extent of the supply chain, some firms will want to have the necessary internal resources to manage this process. Like much in life, good communication is crucial.

**ESG expectations and compliance have moved well beyond the "green washing" early phase of the movement.** Consumers, investors, partners and the planet will be watching how companies' approach and live up to ESG goals. Companies need to focus on their supply chain to ensure they can meet ESG goals. The challenges of ESG is in large part because to meet these goals, your business requires visibility and understanding of what is happening within the network. With 60% of companies reporting they lack total visibility of their supply chains, the ability to properly meet your ESG compliance is a daunting task.[8]

**You can't manage what you can't measure. For ESG compliance needs this is core.** Companies need to understand their supply chains, clearly communicate their ESG compliance and leverage all the necessary data to meet their ESG needs. Start with your data strategy - internal and external data, to paint the clearest picture of your supply chain.

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[8] *https://financesonline.com/supply-chain-statistics/*