

The Modern Slavery Act:

How do you respond to new obligations whilst also making the most of new opportunities?



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As a key human rights risk for many businesses, modern slavery continues to be a serious problem both in operations and supply chains. Latest estimates suggest that over 40 million people are currently subject to forced or bonded labour or servitude. This historically under-regulated area is now subject to mandatory reporting in Australia.

Modern slavery includes the crimes of human trafficking, slavery and slavery like practices, such as forced labour, the sale and exploitation of children, and bonded labour. The most common form of modern slavery in corporate supply chains is bonded or indentured labour that occurs through the exploitation of vulnerable migrants who are subject to debts from labour recruitment fees.

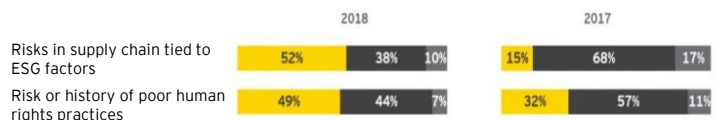
Since the experience of apparel companies in the 1970's - 1990's, businesses have been aware of the risks to brand value and reputation, as well as risks to security of supply when serious labour rights issues are uncovered. Only recently have organisations become more aware of the volume of labour rights issues, both in extended supply chains overseas and shorter supply chains (e.g. within agriculture) on-shore in Australia, as well as within the engagement of labour hire. Consumers, the media and NGOs were outraged with the apparel companies in the 1990's and with management's apparent attitude that a lack of ownership of factories equated to a lack of influence and a corresponding lack of responsibility.

Today we see businesses taking a very different approach. Where organisations have started to see their influential relationships with their supply chain as a trigger for responsibility - the business community and broader stakeholders are seeing these relationships as a crucial opportunity to influence positive change and put an end to modern slavery.

The nature of supplier relationships and actions required to address slavery also lend themselves to improving business operations, security of supply and supply chain efficiencies.

Investors have taken notice of human rights and supply chain risks in their investment portfolios. Not only because of reputational risk concerns, but also due to the understanding that an organisation's commitment and maturity to address environmental, social and governance (ESG) risks is an indicator for overall strong governance, corporate ethics, resilience and long-term value creation potential.

The EY 2018 Investor Survey found that human rights practices and supply chain risks are two areas that saw the most substantial increase in investor attention between 2017 and 2018. In 2018 investors reported that 52% and 49% would rule out an investment due to supply chain ESG risks and human rights practices, respectively.



Although there is a clear case for organisations to review their supply chains to address incidences of modern slavery and build stronger businesses, action to date has been predominantly reactive and isolated to a few market leading businesses.

Australia now has a Modern Slavery Act, which came into effect on 1 January 2019.

The Modern Slavery Act requires disclosure of:

1. The entity's structure, its operations and its supply chains,
2. The modern slavery risks present in the entity's operations and supply chains,
3. The actions taken by the entity to assess and address those risks, including due diligence and remediation processes
4. How the entity assesses the effectiveness of such actions
5. The process of consultation with any entities that the entity owns or controls

The primary purpose of modern slavery reporting is to stimulate transparency and accelerate activity to identify, remedy, and ultimately, prevent incidents on modern slavery. To date, existing efforts have not adequately addressed the scale of the problem, which is why change is now required and encouraged across all levels of the value chain.

The legislation that was called upon by businesses, NGOs and government actors, through a broad consultation process, has demanded a change in the way we do business. It requires a change in policies and processes, but also a shift in mindset and accountabilities. The legislation, and associated consultation process, has significantly raised the visibility of the issue and is set to contribute more positive outcomes than simply compliance-driven transparency.

Requirements of the legislation

The Modern Slavery Act requires mandatory disclosure, by all entities that carry out business in Australia with revenues over AUD\$100m, of the modern slavery risks identified in its operations and supply chains and the steps taken by businesses to identify, mitigate and remedy the risks or incidents. The statement produced will need to be signed off by a Board Director, and as such, will need to fit within formal risk management procedures at the highest level of the organisation.

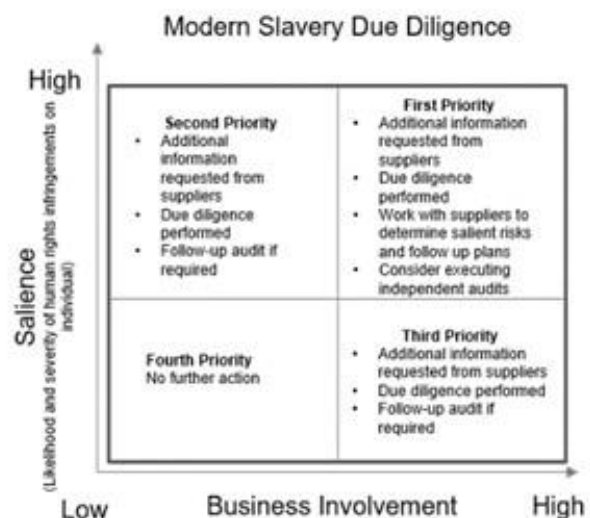
Most organisations will recognise that a public statement, endorsed by the Board, requires demonstrable actions to back it up. Many organisations, including international peers that have been subject to similar legislation for some time, are already embedding due diligence processes to manage modern slavery risks. They are pro-actively addressing the cause and effect of human rights abuses in their operations and supply chains, realising the business benefits provided through greater supply chain transparency and developing stronger supplier relationships. However, for other organisations, the concept of taking responsibility for labour rights within their supply chains will be new and daunting.

Understanding due diligence

Conducting due diligence is about executing controls that are proportionate to, and appropriate for, managing the specific nature of the risks. Due diligence therefore requires an understanding of the risk landscape within the supply chain and devising appropriate controls and responses to address those risks. This may include a framework like this:



Part of this framework will result in segmentation of supplier categories or individual suppliers to help determine the appropriate response. For example:

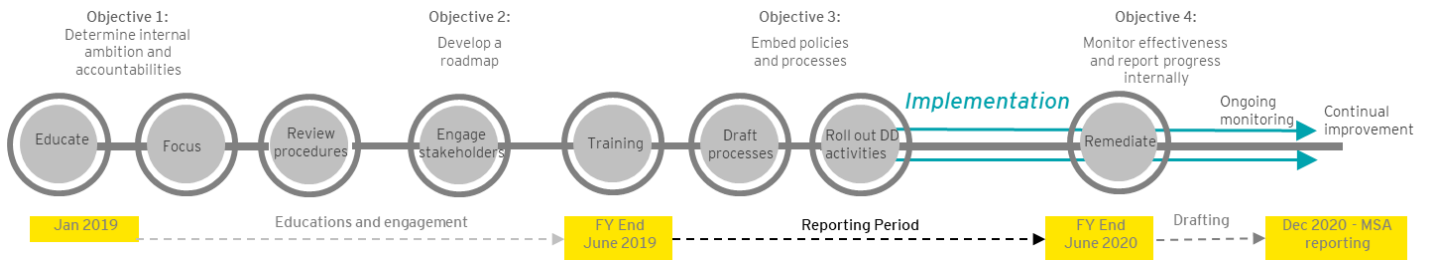


Tailoring responses to the type of supplier risk and relationship can help the organisation to achieve more with its limited resources and focus its activities in a more transparent and risk-based approach.

For many organisations, these changes will take some time to fully embed. However, with the legislation now enacted, we have a timeline set with which to ensure actions are being rolled out, in preparation for the first round of reporting at the end of 2020. The timeline on the following page sets out some of the key objectives and milestones many businesses will be looking to achieve in preparation for producing a meaningful modern slavery statement.

Companies with a 30 June year end will be required to publish a modern slavery statement by 31 December 2020 (6 months after their year-end following a full financial year from commencement).

Planning for Reporting: Indicative timeline outline



Realising the benefits

At an operational level businesses benefit from improved due diligence processes where they have closer relationships with their suppliers and greater transparency over supplier practices.

We are already seeing instances where an ambition to improve supply chain transparency for labour rights has improved supply chain efficiency through consolidation (reducing total numbers of suppliers engaged with). In addition to increases in the quality of engagement through assessments of supplier information and supporting suppliers with training and capacity building.

Strong due diligence frameworks also create a robust governance and accountability structure. Providing company Boards with the information they need to efficiently discharge their fiduciary duties, and use their oversight to motivate change, is a precondition for strengthening the organisation's brand and trusted reputation.

Risks of in-action

Modern slavery will not be eradicated without the voluntary commitment and collaborative efforts of organisations at all points across the value chain.

The greatest risks for businesses is that the pre-conditions for modern slavery continue to exist having a negative impact on the moral, operational and reputational capital of public and private sector organisations.

Beyond moral implications, the financial impacts of a failure to address modern slavery risks should be considered as part of the fiduciary duties of Boards and efficient operational management by the Executive.

The most considerable costs are likely to stem from delayed action and the requirement to play 'catch-up' to peers or to respond reactively to customer, investor, NGO and media expectations without allowing the business adequate planning time. Some organisations have experienced significant operational costs through the need to reactively audit large numbers of supplier factories at short notice following a third party alerting them to human rights infringements. Other examples include costs of taking products off store shelves (responding to customer boycotts), directly employing groups of contracted staff at short notice and paying higher costs for suppliers due to unforeseen factory shut downs. Organisations can also financially suffer from reduced access to finance and share price implications where investors become more active if they do not believe the business is being sufficiently proactive. The Corporate Human Rights Benchmark (CHRB) is being used by some investors to inform investment decisions and in some instances prompt shareholder resolutions.

The solution to these risks is therefore not only action - but early action. Early action enables organisation to meaningfully engage with stakeholders, roll-out training, build capacity within their organisation and adapt organisational strategies around responsible supply-chain objectives. Realising the benefits of early action should be as much of a motivator as avoiding costs of delayed and reactive responses.

Leading practice examples

Identify: Organisations on the front foot in identifying modern slavery risks have trained front line and procurement staff to include modern slavery risk considerations as part of pre-qualification supplier questionnaire and interview processes. This includes strategic decision making relating to new country entry and expanding product or production lines.

Assess: Businesses are utilising data collected through self-assessment questionnaires and front-line team observations to compliment publically sourced information (e.g. the Global Slavery Index) to risk assess large numbers of suppliers to segment procurement category groups for further due diligence attention.

Mitigate: The most effective mitigation activities are those that focus on building strong relationships with suppliers to improve supplier capabilities and to better understand their needs, limitations and those of their workforce. Involvement or leadership in industry specific forums (e.g. those for cotton and regional specific garment manufacture) are demonstrating progress in affecting systematic change and positive impacts on the workforce.

Remediate: Like mitigation, the most impactful remediation activities do not occur in isolation. Partnerships between the private sector and NGOs are proving to be very effective in supporting grievance mechanisms, and facilitating payment of withheld wages. Some businesses are addressing remediation by directly employing survivors of modern slavery.

Leaders are also leveraging mobile technology to support both mitigation and remediation activities. Mobile applications are helping to provide a 'worker voice' by providing a feedback mechanism from the supply chain to a partnership of an NGO and Retailer. Given the highly sensitive and yet inevitable nature of uncovering victims of modern slavery, all businesses should have a policy approach that assigns accountability, notification and escalation processes that are centred on prioritising the safety and wellbeing of the worker and include notification of third parties and authorities as appropriate.

Monitor and Improve: Leading organisations are embedding supply chains (and modern slavery) risk factors within corporate risk registers to ensure formal monitoring, reporting and escalation of risks and progress to mitigate risks. Larger organisations are benefiting from digital risk management platforms that generate automatic risk status reviews and updates. However, organisations of any size will benefit from formal accountability and risk review frameworks.

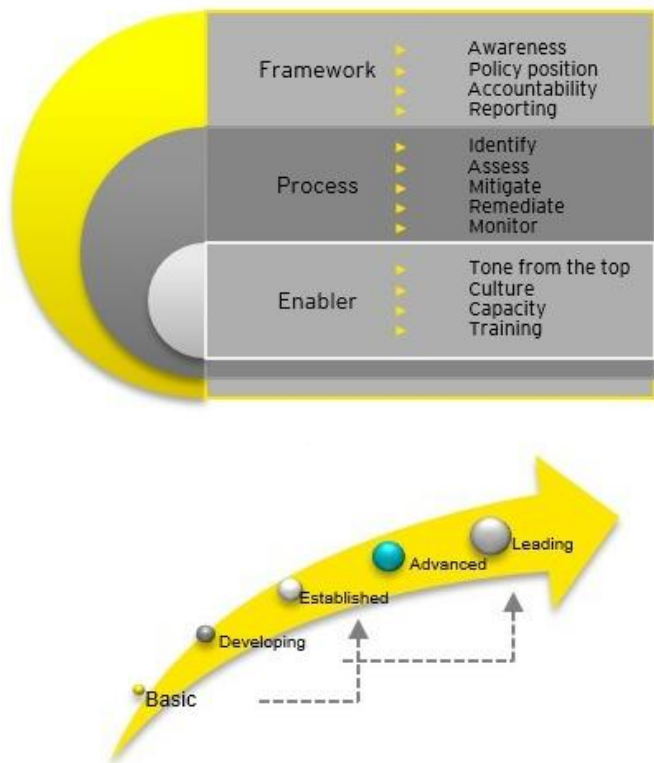
It is important for all organisations to recognise that supply chain risk management is an evolutionary process and will require review and adjustment as the business learns and adapts to its risk environment.



Where to start?

Determining where to start and where to focus efforts will depend on the level of oversight or maturity that an organisation has in supply chain transparency and risk management. Prioritising efforts in the short term will also depend on where the organisation can have the largest impact and what opportunities exist to leverage technology, collaborate with peers and NGOs, and take advantage of existing strengths or address certain process weaknesses within the organisation.

Having worked in this space for some time EY have experience working with, and are closely familiar with the leading practice examples that are emerging in Australia and abroad across a range of sectors. Utilising this experience, we have designed a maturity assessment model that reflects three groups of benchmarking criteria (Framework, Process, Enablers). The model helps organisations assess their current maturity in supply chain risk management, relative to where they want to be, based on their own unique risks and opportunities.



The output of the maturity assessment helps provide a clear roadmap of the considerations and activities that enable a business to progress its maturity overtime, and to respond to its specific risk areas. It helps answers many of the questions that organisations just starting out tend to ask: 'what can we meaningfully do with our limited resources?' and 'where should we focus our attention? Whilst also supporting more mature due diligence frameworks that seek to answer: 'when do we need to do site audits?' and 'what do we do when we discover high risk areas?'

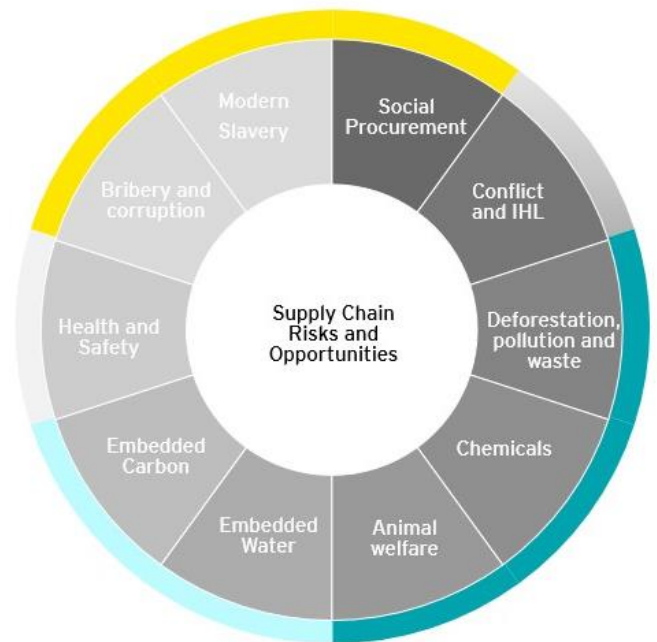
This maturity assessment process has also been designed to support the businesses in considering each criterion to be reported against under the Modern Slavery Act, including identification of risks, due diligence and remediation processes and monitoring the effectiveness of actions.

Looking further across supply chain ESG factors

EY's maturity model has been developed in a way that is flexible to the scope of the challenge different organisations face, and therefore integrates other environmental, social and governance issues that could be relevant to business' supply chains.

Not all areas will be relevant for every business. The maturity assessment methodology facilitates a process to consider the relevance of each issue whereby the business will determine where on the maturity curve it should sit for each issue.

For some industries particularly, those relating to food production, embedded carbon and embedded water are becoming a critical consideration in supply chain decision making. Other industries such as Fast-Moving Consumer Goods (FMCG) are starting to focus more on chemicals within the supply chain, as well as the ever-present modern slavery and labour rights risks. Property, construction and extractives meanwhile are starting to look more at Social Procurement (especially indigenous procurement), with anti-bribery and corruption as well as health safety being the more-mature areas that have been central to many procurement frameworks for some time.



The integrated model enables a highly efficient maturity assessment and provides a road map to improve performance on topics most relevant to each organisation. 'Basic' for one issue may be appropriate if the risk and opportunities are very low or lack relevance. Whereas for another area the business may seek to be leading, where the issue and opportunities align most closely with their operations, strategy and values.

We understand that responsible procurement is increasing in importance for organisations and is seen as a reflection of business ethics and culture. Although understanding responsible procurement risks and opportunities can appear complex for many business, particularly those with diverse operations, it is also critical that these risks are managed and communicated with transparency.

Call to action

Now is the time for organisations to review risks and opportunities within their supply chains. The Modern Slavery Act provides a crucial prompt to start looking at how to adapt businesses processes to better manage these risks - but to also consider how these processes can concurrently respond to other risks and opportunities such as embedded carbon or social procurement objectives.

Identifying priority areas will require cross-functional collaboration, as will determining how business strategy and other business functions adapt to improve opportunities and minimise business risks.

EY welcomes the opportunity for a discussion with you about the priority areas to improve the sustainability of your supply chain, and especially to adapt business processes to respond to modern slavery risks within the legislated time frames.

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