



Integrated Supply Chain – Global Supply

Supply Chain Social Responsibility (SCSR) *Services & General Procurement Suppliers*



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IBM Corporate Citizenship

Corporate Citizenship / Responsibility – defined as:

The way that companies manage their business processes to produce an overall positive impact on society.

Corporate Citizenship is a business imperative

Corporate Citizenship is a platform for doing business in a globally integrated world

- Manage the challenges of globalization
- A key competitive differentiator
- Enabler to opening up and gaining share of new and growing markets
- Relate to more diverse key stakeholders (Communities, NGOs)
- For IBM, consistent with our Core Values

Corporate Citizenship is an increasingly important decision criteria for customers, partners and investors



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IBM Supply Chain Social Responsibility

IBM Supply Chain Social Responsibility (SCSR)

- SCSR is part of IBM's Corporate Citizenship activity

- SCSR is a requirement for all IBM suppliers
 - Supported by the Chief Procurement Officer and Procurement managers/staff

- Suppliers are viewed (externally) as an extension of IBM's brand
 - Supply chains are visible; the Internet makes this possible

SCSR – The IBM Brand

What is at Stake ?

IBM is the world's 2nd most valuable brand... IBM's brand value increased by 30% in 2009 to \$86 billion₁.

₁ Millward Brown Optimor Top 100 Brands 2010

How Does Procurement Protect the Brand ?

"SCSR is not optional, it is a requirement for IBM suppliers. IBM has the second most valuable brand name in the world and we can not have supply chain issues that impact our brand's perception in the market"

John Paterson, Chief Procurement Officer

SCSR – Code Provisions

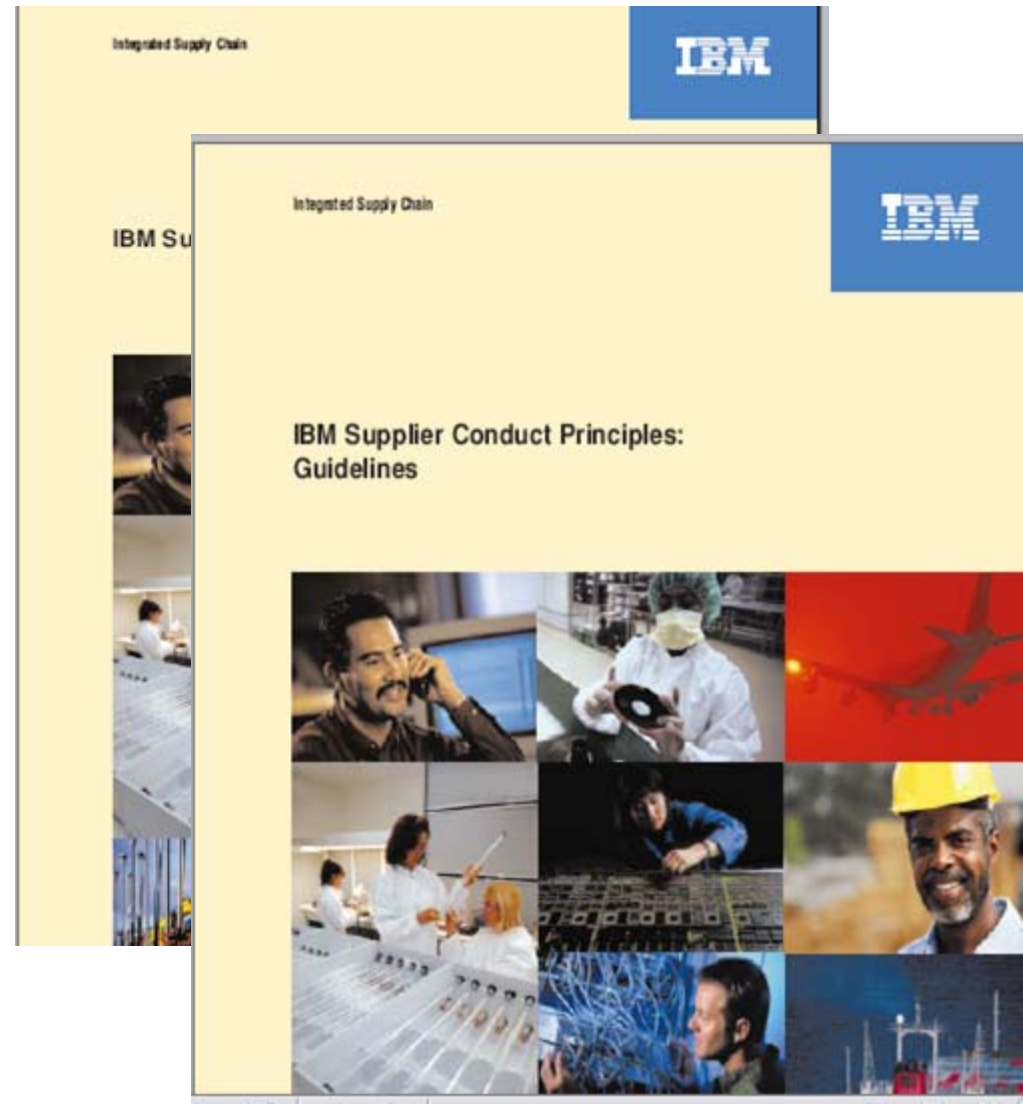
- Requirement for all IBM suppliers
(contained in -> Supplier Conduct Principle Letter Agreement)
- IBM Supplier Conduct Principles address the following 13 provisions
- EICC (industry code) adds +2 Management System provisions
- IBM has adopted the EICC code as equivalent to its own code

1. Forced or involuntary labor
2. Child labor
3. Wages and benefits
4. Working hours
5. Nondiscrimination
6. Respect and dignity
7. Freedom of association
8. Health and safety
9. Protection of the environment
10. Laws, including regulations and other legal requirements
11. Ethical dealings
12. Communications
13. Monitoring/record keeping

IBM Supplier Conduct Principles

- Forced or Involuntary Labor
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SCSR Audit Program

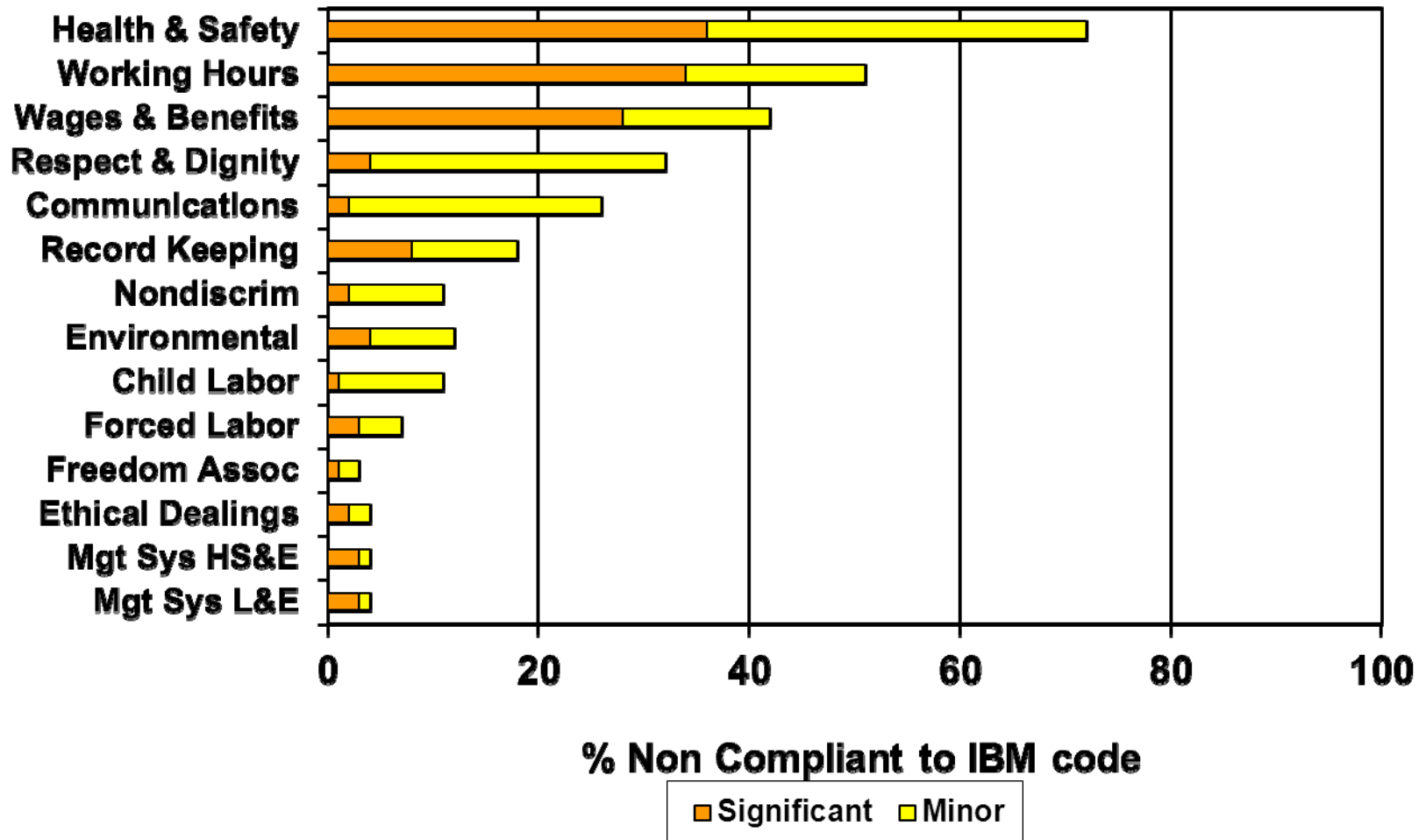
SCSR Audit Program

- IBM Procurement and Supply Chain Social Responsibility team determine suppliers to be audited
- Third party audit firm contracted for the assessments
- Audit report provided to IBM; results to supplier from IBM
- Supplier Improvement Plans (SIPs); reviewed/accepted by SCSR team
 - All improvements must be implemented within 6 months
- Re-audit sustainability 6 months after implementation of SIP
- Monthly internal review of results and SIP acceptance timeframe
- Expectation is for suppliers to be fully compliant with no major nonconformances to Code of Conduct
 - Future business is contingent on this

Supplier Initial Audit Results – Global Cumulative (2004-2010)

Argentina, Brazil, China, Czech Rep, Hungary, India, Korea, Malaysia, Mexico, Philippines, Poland, Romania, Singapore, Slovakia, Taiwan, Thailand and Vietnam

(base = 900+ suppliers)



SCSR Audits: Observations

- A number of issues are seen in emerging market countries:
 - Health & Safety
 - Working Hours
 - Wages & Benefits
 - Management systems are weak relating to social responsibility and laws/regulatory compliance
 - Corporate Citizenship remains a new concept
- Some issues are pervasive and country-specific

Supplier Audits – Best Practices Noted

- Senior Management directly involved in corporate responsibility
- Plans in place to reduce working hours to IBM / EICC limits
- Detailed pay stubs with full disclosure of calculations
- Open management – worker communication channels
- Written policies on HR, Health & Safety, Nondiscrimination, Ethics
- Frequent health and safety worker re-training
- Management systems include all elements of the Supplier Conduct Principles



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SCSR Audit for Services & General Procurement Suppliers

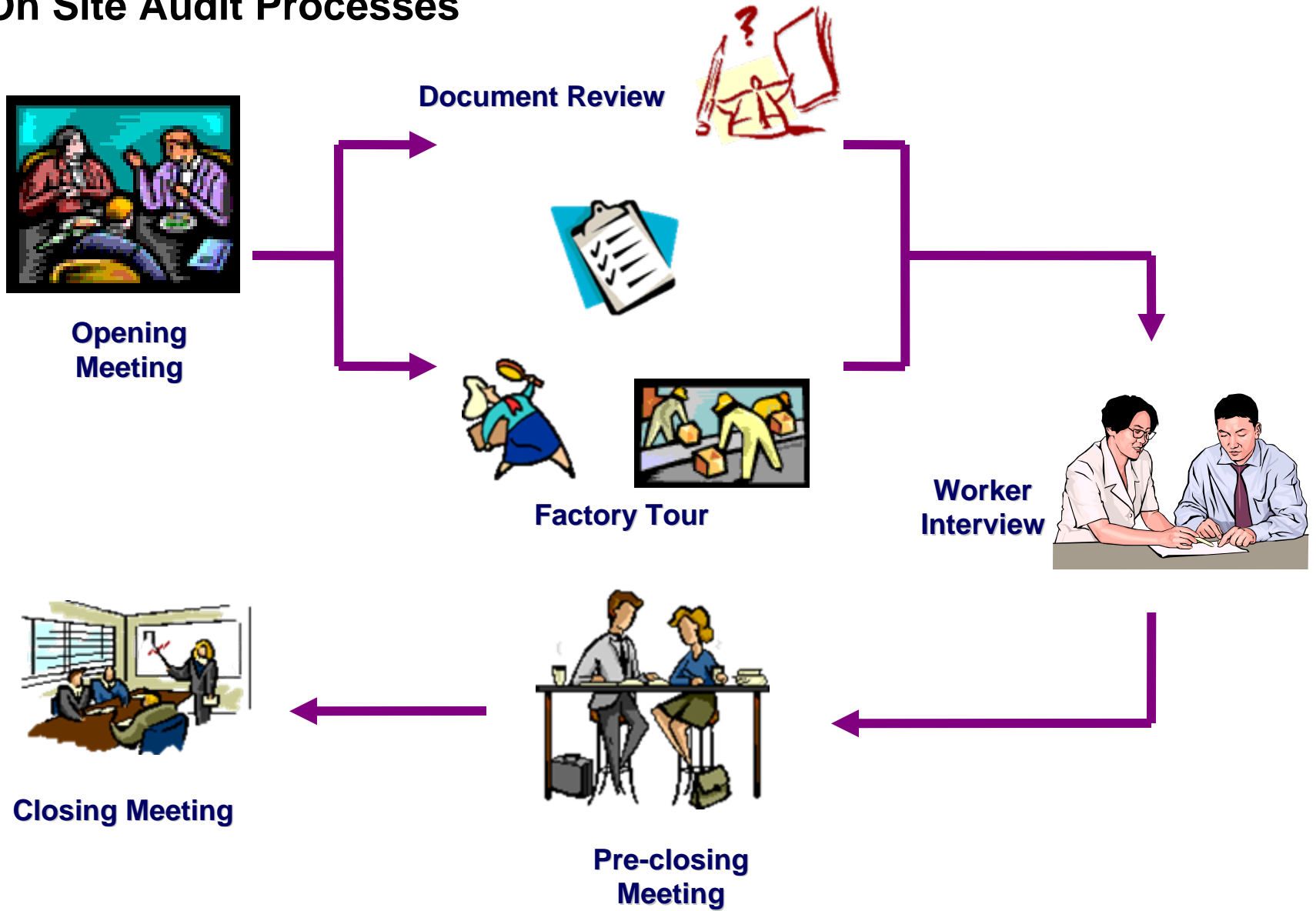
Supplier Audits

- Suppliers audited on all 13 provisions of the IBM Supplier Conduct Principles
- Audits will take place respecting the prevailing laws on data privacy for personal information
- IBM seeks an open audit environment in order to help suppliers identify any areas needing improvement
- Continuous improvement and sustainability are required
- Audits conducted by 3rd party audit firm

Pre-audit Process

- Supplier informed of audit by IBM (SCSR team)
- IBM (SCSR) receives supplier Facilities Identification form;
IBM (SCSR) checks information and forwards to 3rd party audit firm
- 3rd party audit firm contacts IBM's supplier
 - Confirm an audit date, review audit logistics
 - Telephone call
 - E-mail from Facility Identification form
 - All issues with document disclosure worked out
 - Non-Disclosure Agreement, if required
- Audit confirmation
 - Supplier emails their Confirmation Form to 3rd party audit firm
 - IBM is notified of audit date
 - Last minute supplier requests to postpone audits - IBM procurement senior management will be notified

On Site Audit Processes



Opening Meeting

Objectives:

- To get to know each other
- Verify facility information
- Explain the purpose of the audit
- Brief on the standards and requirements
- Introduce the audit procedures



Supplier Document Review

- Personnel files
- Employees labor contracts
- Labor policies
- Business registration/license
- Payment records
- Working hours records
- Health, Safety and Environment documents
- Employee handbooks, Internal rules, Collective agreements, etc.

- * *IBM expects all documents requested by auditor to be provided* *
- * *No copies of documents will be taken, only viewed by auditor* *

Supplier Document Review

- Wages and Working Hours Testing
 - minimum wage
 - overtime rate
 - withholding deposits
 - delayed wages payment
 - wage deductions
 - normal working hours
 - overtime hours
 - number of rest days
 - subcontracted labor policies & practices

Worker Interviews

- Representative sample selected from personnel list and during facility tour (different work areas, ages, gender, races)
- Auditors select the sample of workers; contractors also included
- Private interview needed
- With consent of the employee himself/herself
- Confidentiality of information respected

Facility Tour

- Observe working conditions
- Verify supplier's policies and procedures are practiced
- Select employees for interviews

Facility Tour - Health & Safety

■ General Conditions

- Lighting
- Ventilation
- Structure
- Handrails
- Housekeeping
- Clean toilets
- Drinking water



■ Communications

- Evacuation drills
- Employees trained in emergency response

■ First Aid

- Sufficient number of fully equipped first aid kits
- Records kept for work related injuries

Facility Tour – Health & Safety

- Emergency Preparedness
 - Secondary exits
 - Exits and pathways unblocked
 - Exits marked
 - Exit doors open outward
 - Exits and exit routes of sufficient width
 - Evacuation plan posted
 - Fire extinguishers
 - Appropriate
 - Serviced
 - Marked and mounted
 - Fire alarm
 - Emergency lighting

Facility Tour – Health & Safety

- Worker Safety
 - Chemical storage and labeling
 - MSDS
 - Personal protective equipment where required
 - Chemical, fire, electrical hazards
 - Machine guarding
 - Safe work practices

- Canteen and Dormitories
 - Inspection certificates
 - Housekeeping
 - Adequate space

Facility Tour

- Environmental Assessment
 - Chemical storage and handling
 - Liquid waste disposal
 - Solid waste disposal
 - Air pollutant exhaustion

Closing Meeting

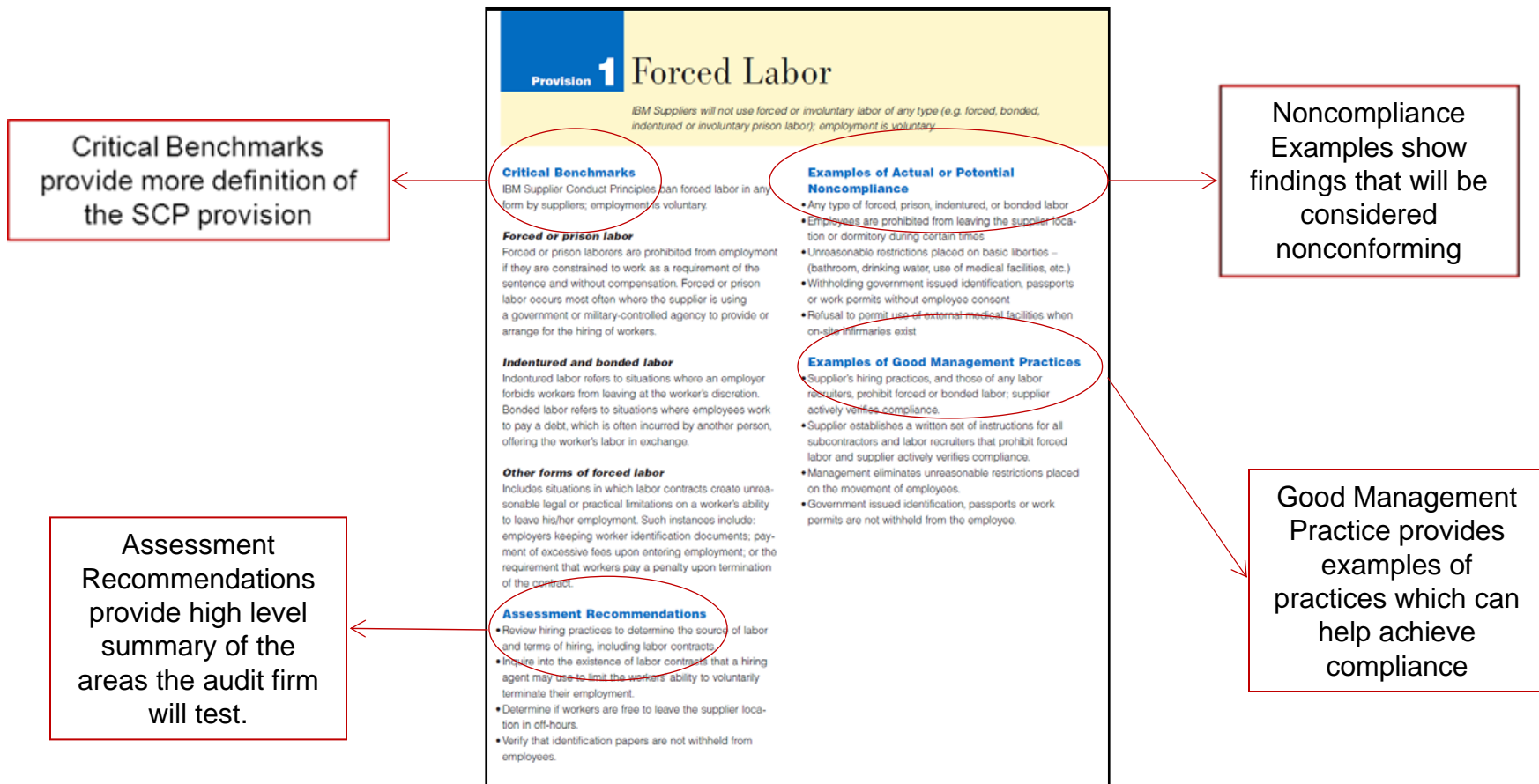
- Explain reporting process: 3rd party auditor > IBM > Supplier
- Provide high level findings summary
- Resolve any supplier questions from the audit
- Provide contact information within 3rd party audit firm

Common IBM SCSR Audit Compliance Findings (Emerging Markets)

- Access denied to wages documents and/or worker interviews
- Lack of written policies (i.e. Child Labor, Forced Labor, Non discrimination, Abuse and Harassment)
- Policies and procedures not communicated to employees
- Incomplete health and safety programs
 - Worker training not documented
 - Incomplete injury logs
 - Emergency egress conditions, no evacuation drills
 - Personal protective equipment not used, unguarded equipment
 - Hazardous materials without proper labels or not properly stored
 - First Aid – No training, first aid kits not properly equipped, no eyewash stations
- Overtime hours not paid at legally mandated rates
- Unreliable overtime tracking
- Lack of effective internal monitoring to ensure SCP compliance

Additional Audit Preparation – Review the Supplier Conduct Principles Guidelines

www.ibm.com/procurement select “Supply chain social responsibility”



These guidelines are not an exhaustive list, by any means. Our suppliers are responsible for complying with IBM's Supplier Conduct Principles, period. But we do think that by publishing this document, we will help our suppliers benchmark their existing performance and establish internal improvement plans.



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Supplier Improvement Plan Guidance

Supplier Improvement Plan Guidance

- Supplier Improvement Plans (SIP) is required in response to audit findings
- SIPs are used to effectively address audit findings by focusing on the development and implementation of management systems, processes, and worker - based knowledge
- Health & Safety issues should be given immediate priority
- All SIPs must have an 'owner' assigned implementation responsibility and address the cause of the nonconformance.
- "Root Cause Analysis" is a method used to understand the initial cause and subsequent causal events leading to the nonconformance. It is used to correct or eliminate the cause, and prevent the problem from recurring.
- If a Root Cause Analysis is not conducted, or conducted poorly, there is a risk that time and resources will be wasted addressing the symptoms of a problem, rather than addressing the real issue.
- SIPs need to be provided to IBM within 30 days of report summary receipt
- All actions must have implementation within 6 months
- Each action will be re-assessed to determine effectiveness
- Expectation is 100% compliance for continued IBM business

Root Cause Analysis

- The most common element of a Root Cause Analysis is to ask “why a particular problem or nonconformance occurred?” and document the answer. The process may require asking “why?” several times to identify the causal events and relationships associated with the nonconformance. It might be useful to consider the following potential elements to ensure comprehensive analysis:
 - Knowledge – did the problem occur due to lack of awareness or knowledge?
 - Assignment – did the problem occur because responsibility(ies) was not clearly assigned?
 - Tools – did the problem occur because appropriate tools were not available?
 - Training – did the problem occur due to lack of proper training?
 - Accountability – did the problem occur because of little/no accountability, e.g., in a typical situation nothing happens when the task is not done?
 - Resources – did the problem occur due to insufficient resources?

Reporting Progress

- Suppliers are expected to implement improvements in the manner and within the timelines agreed to in the approved SIP
- The supplier is required to keep IBM informed of progress toward the completion of SIP actions
- Any changes to the approved SIP must be reviewed and approved by IBM



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SCSR Resources

SCSR Team:

- John Gabriel (USA) - jmg548@us.ibm.com
 - Corp HQ rep for Corp Citizenship, Chair EICC, SCSR Program Mgr
- Michael McGrath (USA) - mjmcgrat@us.ibm.com
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 - Asia SCSR Regional rep, EICC VAP & SAQ

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 - European SCSR Sourcing Lead

- Eugenia Bravo (Mexico) - eubravo@mx1.ibm.comL
 - Latin America SCSR Sourcing Lead

Resources

- Supplier Conduct Principles & Guidelines
(www.ibm.com/procurement)
- IBM Corporate Citizenship Report
(www.ibm.com/ibm/responsibility)
- IBM's Requirements for Suppliers Regarding a Corporate Responsibility and Environmental Management System
(www.ibm.com/procurement)
- Electronic Industry Citizenship Coalition
(www.eicc.info)