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HOW TO CONDUCT A SUPPLIER AUDIT AND WHY IT IS A GOOD IDEA





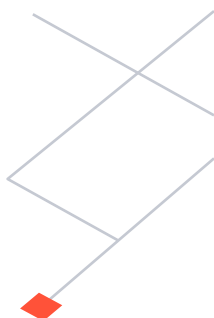
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WHY CONDUCT SUPPLIER AUDITS?

A big part of successful supply chain management is getting good information about the players involved. Your company probably has hundreds of suppliers, perhaps even thousands. How do you know which ones are actually able to deliver what they've promised?

Supplier Audits are a good way to verify that any given supplier is in a position to produce the products or services they've been contracted to deliver, on time and on budget. An audit can also gather other specifics that might be important to your company, different information such as financial stability, quality of goods, brand reputation, and corporate responsibility and governance.

Audit results can and should be put to good use, too. Recognizing positive results can encourage and motivate your suppliers, and even reinforce your brand messages with your customers. Negative results can indicate where suppliers need to improve or in more extreme cases, identify which suppliers should be eliminated. In every case, aggregating results allows you to build and maintain supplier rankings that give a more complete picture of your supply chain's strengths and vulnerabilities.



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HOW TO ENGAGE SUPPLIERS IN AN AUDIT

As with any assessment of performance, communication is key and the more of it the better. Begin by letting all affected suppliers know that you plan on auditing them and what information you will be looking for, being as specific as possible. You'll also want to assess how aware suppliers are of their own capabilities so ideally you would have them fill out the audit form to self-assess, using the same criteria you will be using.

Finding out where the supplier thinks they are weak or strong and comparing those results to your own assessment can be even more revealing than any numbers they may supply. Suppliers typically have an overly generous opinion of their performance. But suppliers that are committed to improvement will do more than just talk. They'll actually demonstrate more of a willingness to provide better services and will work harder to do so.

In all cases, plan on sharing and comparing the results with your suppliers and giving them feedback on how your results compare with theirs. For suppliers who are overperforming, prepare to acknowledge their contributions and if possible, incentivize those behaviors. For clients that didn't quite measure up, set a plan and timeline for them to correct those negative aspects of their performance, and lay out specific consequences should they fail to do so.





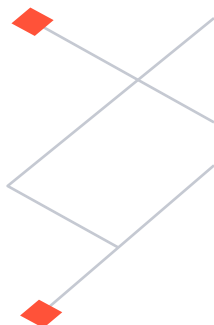
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WHAT SHOULD AN AUDIT COVER?

The beauty of an audit is that it can be used to look for different issues and you get to decide what they are. If it's a new supplier, for instance, you may want a more complete inspection to evaluate all parts of the business. Suppliers with longer term relationships may only need to disclose substantive changes since the last audit.

Depending on a supplier's location, you may want to consider appropriate levels of inspection to your audit. Of course, you want to make sure that a supplier is able to produce consistent quality goods, but you will also want to make sure that the agreed-upon procedures used to produce those goods are being followed as well. And of course, those and all agreements and specifications should be spelled out in writing.

Finally, understanding who's going to be looking at and evaluating the audit results will dictate the level of granularity of information you need. Your finance people will want to see one set of information, while production people will need another. Knowing those demands going in will make the difference between a successful conclusion and an ongoing headache for everyone concerned.



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HOW TO DESIGN AN AUDIT FOR SUCCESS

Results will be as variable as the suppliers they came from, but your criteria must not be: You need to be absolutely clear about your criteria and be able to apply it uniformly. For instance, certain aspects may be deemed absolute and can be graded on a pass/fail basis. Undocumented labor or children working in a factory might be just two conditions that would automatically cause a supplier to fail an audit.

Other criteria can be graded on a scale that incorporates levels or points that are accumulated towards a baseline passing. Having clear documentation for employee safety training is nonnegotiable, but the frequency of employee training can be graded on a sliding scale that also reflects efficacy and testing. In other words, evaluation criteria should not vary, but how that criteria are evaluated may. As always, beginning with the end result in mind and understanding what you're looking for and why it's important to you helps ensure you're collecting information that matters.

And in that regard, you'll want to ask questions that have straightforward answers. For instance, here are some things you may want to know:

- How many locations does the supplier have?
- What's the capacity of their factories?
- How many days are they in use?
- What types of labor are performed there?
- Are there any contingency plans for various kinds of disruptions?
- What kinds of quality programs are in place and how do they work?
- Do they include incoming and outgoing quality checks?
- What kinds of ongoing employee training programs are available?

And so on. This is obviously not an exhaustive list, and your list will vary considerably depending on the supplier and your business. The point here is to remember to make your inquiries as specific and direct as possible so the answers can be graded on a scale everyone understands.





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HOW TO MEASURE RESULTS

Subjective audit results are typically measured on tiers of success. But again, the guidelines for scoring need to be explicit and understood by all parties, with clear criteria separating one tier from another.

For example, on a scale of 1-5 with 1 being the worst...

1. Doesn't respond most of the time; usually doesn't answer within 24 hours
2. Regularly doesn't respond to email/phone calls with inconsistent follow up
3. Responds to most correspondence and always within 24 hours
4. Responds within business day and follows up on outstanding items
5. Proactively reaches out; response is never an issue

Likewise, a clear and easy to understand system for aggregating scores and the respective results is essential. As mentioned above, a provision for criteria that encompass a range should be factored in and clear policies put in place to incorporate their impact, i.e. what is the lowest grade that is acceptable and do certain measurements carry more weight.

For instance, here are some some key considerations, or KPIs, and their possible measurements:

1. Quality controls in place with track record? Measure the percent of defects within a certain time period.
2. Available capacity to meet needs? Look at the applicable machine rates, total days worked, efficiency rates.
3. Contingency plans? Measure machine capacity, and whether alternate manufacturing sites are available.
4. Fair labor practices, employee safety measures? Make sure the supplier has the proper certifications, Environment, Health & Safety documentation and employee training programs in place.
5. Multiple locations? Is the same equipment in place at different locations and are their available personnel there to run it according to agreed upon rates.
6. Responsiveness? On a scale of 1 to 5, how responsive is the supplier's organization?

Here again, your key considerations will be different, but these samples should provide an idea of what to look at and how the performance and results should be measured.



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KEY CONSIDERATIONS OF A SUPPLIER AUDIT



Key Considerations of a Supplier Audit

- ✓ **Quality controls in place with track record**
Percent of defects within x time period
- ✓ **Available capacity to meet needs**
Machine rates - Total days worked - Efficiency rates
- ✓ **Contingency plans**
Machine capacity - Alternate manufacturing sites
- ✓ **Fair labor practices & employee safety measures**
Certifications - EH&S documentation - Employee training
- ✓ **Multiple locations**
Same equipment at different manufacturing locations
- ✓ **Responsiveness or response rate**
Does the organization respond in a timely manner



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AUDITS CAN BE A SUCCESS FOR EVERYONE

There are many reasons why you might want to conduct supplier audits, but there is only one way to conduct a successful one: with openness, honesty and plenty of clear, upfront communication. Understanding the questions that are most important to be answered is only the first step. You must also be able to accurately measure the results of those questions against objective criteria and have a plan for providing the appropriate feedback.

Conducting supplier audits is simply a good business practice and can yield valuable insights for everyone involved. To the extent that goal is accomplished should be your own measurement as to whether your supplier audits are successful.

For more information about how we can help improve almost every aspect of your supply chain management, including our own list of audited and ranked supplier recommendations, visit www.anvyl.com.

