



## SME-tailored due diligence

### Objectives of the session

- Share findings from recent OECD research on sourcing and due diligence practices of SMEs operating in the garment and footwear sector.
- Identify successful SME-adapted due diligence practices; Hear from SMEs on approaches they are taking and the related outcomes, opportunities, and challenges.
- Discuss in what ways policy developments on due diligence can ensure appropriate SME inclusion, and what complementary measures (tools, resources etc.) can be put in place to support SME's due diligence implementation.

### Background

#### What is the context?

SMEs are predominant actors in the global garment and footwear sector, where they are prevalent across the whole supply chain. While they constitute the backbone of the sector, their resources, knowledge and capacity to implement due diligence tend to be more limited compared to larger multinationals. A session was held at last year's Forum on [engaging SMEs to scale responsible business practices](#), focusing on their importance for increasing uptake of due diligence practices as well as addressing some of the real and perceived challenges they may face.

Identification of particular barriers and challenges to due diligence for SMEs is necessary to:

- determine in which instances SMEs may choose to use a different approach, compared to large enterprises, to implement due diligence;
- identify successful SME-adapted due diligence practices
- develop effective tools for the different stakeholders to support and facilitate SME due

diligence implementation<sup>1</sup>

This is also needed in order to have an informed discussion regarding the appropriate inclusion of SMEs in RBC policy and regulation developments. To date, more attention has been paid large companies as frameworks on due diligence and responsible business practices are largely developed for multi-national enterprises. Reporting instruments focus initially on large companies, and legislative efforts often exclude many SMEs from mandatory reporting by establishing minimum thresholds based on financial turnover or staff size, while compliance might be required as suppliers of larger enterprises. Yet the prevalence of SMEs demonstrates the need to understand and address their social and environmental impact.

Therefore SME inclusion is at the centre of the debates about mandatory due diligence, particularly how to ensure proportionality and reasonableness of requirements and accountability. Governments have a role to promote coherence and address unnecessary barriers that impede the implementation of RBC standards by businesses, and this will be particularly relevant in the case of SMEs.

Company category	Staff headcount	Turnover	or	Balance sheet total
<b>Medium-sized</b>	< 250	≤ € 50 m		≤ € 43 m
<b>Small</b>	< 50	≤ € 10 m		≤ € 10 m
<b>Micro</b>	< 10	≤ € 2 m		≤ € 2 m

## What progress has been made?

While more attention has been paid to large companies, there are a growing number of examples of good SME due diligence practices supported by diverse actors, involving training, raising awareness, and understanding and providing technical support to incentivise RBC, as well as to supporting implementation among SMEs. Organisations such as WWF developed programs to enhance due diligence uptake by SMEs, by engaging with SME owners to help them understand the importance of investments in resource efficient technologies and how they can reap long-term monetary benefits. Other actors such as large businesses have incorporated due diligence support in their business relationships with SMEs, either to develop due diligence awareness among SMEs, with programs that involve training and capacity building when buying from SMEs<sup>2</sup>, or by implementing responsible purchasing practices.

Multi-stakeholder initiatives can also have a very important role in supporting SME due diligence, as collaboration can help reduce costs of due diligence, harmonise assessments and pool leverage - given that two persisting barriers of due diligence implementation are financial capacity and lack of leverage. Multi-stakeholder initiatives can provide tailored guidance to companies working in the garment industry and guide brands through every step of the due diligence process. This is

<sup>1</sup> International Labour Organization (2019), *Small Matter: Global evidence on the contribution to employment by the self-employed, micro enterprises and SMEs*, Geneva, [https://www.ilo.org/wcmsp5/groups/public/---dgreports/---dcomm/---publ/documents/publication/wcms\\_723282.pdf](https://www.ilo.org/wcmsp5/groups/public/---dgreports/---dcomm/---publ/documents/publication/wcms_723282.pdf)

<sup>2</sup> International Labour Organization (2016), *Good Procurement practices and SMEs in global supply chains: what do we know so far? : A literature review*, Lizbeth Navas-Aleman, Tamara Guerrero; International Labour Office, Enterprises Department. Geneva, [http://www.oit.org/wcmsp5/groups/public/---edemp/---empent/---ifp\\_seed/documents/publication/wcms\\_486227.pdf](http://www.oit.org/wcmsp5/groups/public/---edemp/---empent/---ifp_seed/documents/publication/wcms_486227.pdf)

especially relevant for SMEs that often do not have the resources to fully understand the gamut of requirements and implement due diligence strategies and procedures.

Several governments have already put in place tools and resources to support SMEs including stimulation programs that avoid a disproportionate administrative burden for SMEs<sup>3</sup>, increasing SMEs’ due diligence awareness and understanding, but also technical capacity for implementation. For instance the EU has developed a programme under the conflict mineral regulation, “EC SME Support Programme”, with supporting materials including an educational platform, a due diligence toolbox, training modules, and educational webinars prepared as ready-to-use content<sup>4</sup>. In Germany, an SME-targeted programme provided guidance and coaching for SMEs on topics related to RBC; linking businesses to share best practice, and support and guidance to SMEs interested in doing business in developing countries<sup>5</sup>. Canada developed an SME Sustainability Roadmap<sup>6</sup> to assist SMEs in achieving sustainability goals, focused on practical examples. Financial support has also been put in place to incentivise RBC, for example in Indonesia where the government grants SMEs tax reductions and exemptions for pollution control equipment and the cost of water treatment<sup>7</sup>. These can be powerful levers for governments to guide corporate behaviour, promote exchange of best practice on RBC, but also to level the playing field.

### What are remaining challenges/gaps?

SMEs still face significant obstacles when implementing due diligence. An OECD survey conducted last year revealed some of the most important perceived obstacles to SMEs due diligence relate to leverage, financial resources, supply chain visibility and due diligence awareness. All of the challenges are transversal:

LEVERAGE	VISIBILITY OVER SUPPLY CHAIN	FINANCIAL RESOURCES	DUE DILIGENCE AWARENESS
<p>SMEs tend to have lower level of leverage due to their size and the fact that their orders represent a small amount of their supplier’s total production. They are also more likely to be impacted by external factors such as poor purchasing practices</p>	<p>SMEs have capacity, leverage, and resources constraints to implement traceability. They are less likely to engage in collaborative approaches to traceability.</p>	<p>Relative cost of due diligence tend to be higher given their position in the supply chain, leverage over their suppliers and lack of financial liquidity and small margins.</p>	<p>There is low reliance on governments, CSO and trade unions to obtain RBC information. SMEs may have constrained access and understanding to RBC information.</p>

<sup>3</sup> Change in Context, commissioned by Ministry of Foreign Affairs of the Netherlands (2018), *Government policy to stimulate international responsible business conduct*, <https://media.business-humanrights.org/media/documents/files/government-policy-to-stimulate-international-responsible-business-conduct.pdf>

<sup>4</sup> European Commission (2017), Levin Sources and RINA Consulting, *Study on the Support System for SME Supply Chain Due Diligence*, Final Report, <https://www.levinsources.com/assets/pages/report-study-on-the-support-system-for-SME-supply-chain-due-diligence.pdf>

<sup>5</sup> Change in Context, commissioned by Ministry of Foreign Affairs of the Netherlands (2018), *Government policy to stimulate international responsible business conduct*, <https://media.business-humanrights.org/media/documents/files/government-policy-to-stimulate-international-responsible-business-conduct.pdf>

<sup>6</sup> Government of Canada, SME Sustainability Roadmap, [https://www.ic.gc.ca/eic/site/csr-rse.nsf/eng/h\\_rs00174.html](https://www.ic.gc.ca/eic/site/csr-rse.nsf/eng/h_rs00174.html)

<sup>7</sup> Global Partnership for Financial Inclusion, World Bank Group, Federal Ministry for Economic Cooperation and Development (2017), *Financing SMEs in Sustainable Global Value Chains*, G20 Germany 2017, [https://www.gpfi.org/sites/gpfi/files/documents/GVC%20paper\\_highres\\_0.pdf](https://www.gpfi.org/sites/gpfi/files/documents/GVC%20paper_highres_0.pdf)

On the other side, several aspects of SME structure, business relationships, and sourcing practices, provide opportunities for due diligence implementation which is risk-based and tailored to their size and position in the supply chain. While there is movement towards collective support for SME due diligence implementation, gaps remain regarding coordination of action, and efforts will be inadequate if not harmonised.

One of the most discussed gaps remain at the policy level, and concerns the level of inclusion SMEs should be subject to in RBC policy developments. The appropriate inclusion of SMEs will be particularly valuable to ensure a level playing field where SMEs remain competitive while implementing due diligence. This has been discussed in the context of development of regulation to mandate company due diligence. In most cases to date, SMEs have been exempted under these laws<sup>8</sup>.

Some due diligence regulations already include SMEs in their scope and several others currently under review concerning the proportionality and potential impact of SME inclusion. Some suggest their exclusion cannot be justified given the significant impact they can have on the society and the environment, and are already under disclosure pressure by their business partners as SME suppliers. Generally, key questions related to inclusion of SMEs in due diligence regulation points to the relative administrative burden of SMEs (often relatively greater than for larger companies); competitive disadvantage vis-à-vis larger companies and tighter contractual obligations imposed by their large corporate clients; they also appear to lack sufficient leverage to extract the necessary information from their supply chain partners. Civil society tends to seek strengthened regulation of SMEs due diligence practice. While there are differing views on the issue, the evidence case has still to be built proving the impact of the different tools and mechanisms on the improvement of SMEs due diligence performance.

## Discussion questions

- How can SMEs adapt their due diligence practices to their characteristics? What type of recommendations does the OECD Guidance provide?
- What are the common points between different SME approaches to due diligence?
- What are the persisting barriers to SME due diligence implementation? How can the different stakeholders provide support to enhance due diligence uptake by SMEs?
- How to ensure effective SME inclusiveness in RBC policy developments? What tools and complementary measures can governments put in place to ensure a level playing field?
- What mechanisms beyond industry associations, could allow policy makers to directly engage and learn from SMEs?

## For more information

<sup>8</sup>M. R. Pearl S. Suilt (2019), Applicability of Supply Chain Laws to SMEs: A Critique of the Laws of the United States, the United Kingdom and the European Union, Central European University, [https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=&cad=rja&uact=8&ved=2ahUKEwj8KKGyrXuAhUJmRoKHeuQADsQFjADegQIBBAC&url=http%3A%2F%2Fwww.etd.ceu.edu%2F2019%2Fsuilt\\_ricca-pearl.pdf&usq=AOvVaw2Tg-K9G1W8f1Lf33\\_ys4JX](https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=&cad=rja&uact=8&ved=2ahUKEwj8KKGyrXuAhUJmRoKHeuQADsQFjADegQIBBAC&url=http%3A%2F%2Fwww.etd.ceu.edu%2F2019%2Fsuilt_ricca-pearl.pdf&usq=AOvVaw2Tg-K9G1W8f1Lf33_ys4JX)

- OECD Global Forum on Responsible Business Conduct, Session Note on Promoting due diligence, the role of Governments, 2018, <https://mneguidelines.oecd.org/global-forum/2018-GFRBC-Session-note-Role-of-Government-for-DD.pdf>
- ILO SME Unit, *Procurement practices and SMEs in global supply chains: what do we know so far? : A literature review*, Lizbeth Navas-Aleman, Tamara Guerrero; International Labour Office, Enterprises Department. Geneva: ILO, 2016, [https://www.ilo.org/wcmsp5/groups/public/---ed\\_emp/---emp\\_ent/---ifp\\_seed/documents/publication/wcms\\_486227.pdf](https://www.ilo.org/wcmsp5/groups/public/---ed_emp/---emp_ent/---ifp_seed/documents/publication/wcms_486227.pdf).
- Change in Context, Ministry of Foreign Affairs of the Netherlands, *Government policy to stimulate international responsible business conduct*, 2018, <https://media.business-humanrights.org/media/documents/files/government-policy-to-stimulate-international-responsible-business-conduct.pdf>
- European Commission, *Study on the Support system for SME supply chain due diligence: Final Report*, 2018, <https://op.europa.eu/en/publication-detail/-/publication/67a2c448-fb38-11e7-b8f5-01aa75ed71a1/language-en/format-PDF/source-67264534>
- Shift Project, *On Mandatory due diligence, SME's don't need a free pass; they need flexibility*, Francis west, 2020, <https://shiftproject.org/smes-mhrdd/>

### About Shirahime Advisory

Shirahime works with committed companies to become 'future fit', and leverages their influence as a force for good.

Their expertise serves the consumer goods industries, including textiles, as a guide toward the Circular Stakeholder Economy, so as to meet the human rights of every person within the means of our life-giving planet by being a successful company. Shirahime's approach focuses on developing sustainability good practice, knowledge and skills, in corporate boards and at executive level particularly in the SME space, by facilitating long-term strategy processes and strategy translation into tangible action and results.