Junior Kannah via Getty Images

The mining sector in the Democratic Republic of Congo is poorly regulated

PUBLIC RELATIONS

Tread carefully: the art of ESG disclosure

What's the best way for communications teams to manage reputational issues in the supply chain?

Laurie Clarke

When Boohoo was accused of modern slavery in 2020 because of the working conditions in one of its suppliers' factories in Leicester, its share price fell by 18%, retailers dropped the brand and it was facing a possible US import ban. The case was an object lesson in the importance of supply chain due diligence – and handling the communications around it effectively.

Boohoo is far from the only high-profile UK firm to have been caught up in scandal affecting a supplier. Dyson is facing compensation claims alleging that working conditions in a Malaysian factory were unsafe and exploitative. Tesco, meanwhile, is dealing with a class-action lawsuit brought by workers at a Thai factory that made garments for its F&F brand until 2020.

Companies have long been aware that the blowback from ESG-related failures in supply chains can eviscerate reputations, incur fines, trigger lawsuits and, in the most severe cases, end operations entirely. As consumers become more ethically conscious and regulatory bodies strengthen their rules, the stakes are rising. How, then, should companies communicate their ESG due diligence and if the worst-case scenario arises where an ESG-related failure is discovered in the supply chain, how should they respond?

"Transparency and honesty are crucial," says Helen Ellis, head of consulting at Team Lewis, a marketing and communications agency. "It's important to own a mistake. Ultimately, it comes down to trust and honesty; it's about trying to very quickly say, 'Yes, this has failed'. Then it's about communicating and explaining what you're going to do differently going forward."

Alex Harrison, co-head of projects and energy transition at law firm Akin Gump, agrees. "It's not the crime. It's the cover-up. At its heart, ESG is about integrity. A company that discovers a supply chain issue should look to be as open and honest as it can be about the problem."

But Harrison counsels against rushing out a statement, beyond acknowledging the problem and a willingness to respond to it appropriately. "A company may not have all the facts, or its suspicions may be disputed or unfounded... the company may not be free to disclose all the information available to it for legal or regulatory reasons." Instead, a balanced account of what a company does or does not know (and is able to share), may be the best approach; what is paramount is not burying one's head in the sand.

Perhaps more important than acknowledging and communicating about the incident itself is the action that companies take afterwards – and how that is communicated. The widely publicised 2013 Rana Plaza disaster in Bangladesh, where an eight-storey commercial building housing five garment factories collapsed, was a major turning point for not just one company, but for the whole fashion retail industry.

Companies banded together to create associations coordinating their efforts to address the problems highlighted by the incident. Some of the measures taken included overhauling supplier auditing practices, including broadening the scope of what was included in an audit to cover, for example, the safety of factory infrastructure and workers' rights. Companies also started to invest more in their suppliers, transforming a purely transactional relationship into a more collaborative one.

Talking publicly about the steps you're taking to improve can be a good response in the weeks, months and even years following an ESG scandal in your supply chain. After all, the questions won't stop once you've made a commitment to improve: companies will face scrutiny on whether they have followed through.

Take the Boohoo example. "Boohoo quickly sought to rebuild consumers' trust," says Ryan McSharry, UK head of crisis and litigation at international PR firm Infinite Global. "It launched a QC-led investigation of its supply chain, hired an independent factory auditor and announced the creation of its own 'model factory' that would demonstrate best practice in terms of workers' rights."

A 2022 report highlighted progress in Boohoo's work on its supply chain in terms of sustainability and ethical compliance. But two years on from the scandal breaking, activists and shareholders are still criticising the company for alleged low wages, and the lack of repayment of historically underpaid wages.

Some brands try to get ahead of supply chain-related accusations through complete transparency. But clumsy messaging can result in accusations of hypocrisy. When the self-billed ethical brand Tony's Chocolonely publicised 1,701 incidents of child labour in its supply chain, it said that this openness was supportive of its aims of discovering and eradicating child labour and slavery in its business. Instead, the revelation led to criticism, such as from Ayn Riggs, founder of Slave Free Chocolate, who said that Tony's was "pitching virtue to consumers" while engaging in bad practices.

> Transparency and honesty are crucial. It's important to own a mistake

But transparency can only go so far. Mercedes-Benz has published information about its sourcing of cobalt – the element used in electric vehicle (EV) batteries – which is mined in the Democratic Republic of Congo (DRC) under conditions which often violate human rights guidelines. The company has claimed to be committed to the goal of only using "certified" mining sites that have undergone auditing but in practice it is incredibly difficult to avoid this problem when buying cobalt from the DRC.

Tesla is now focused on the production of batteries which are cobalt-free. This new pivot could help reduce the cost of EVs.

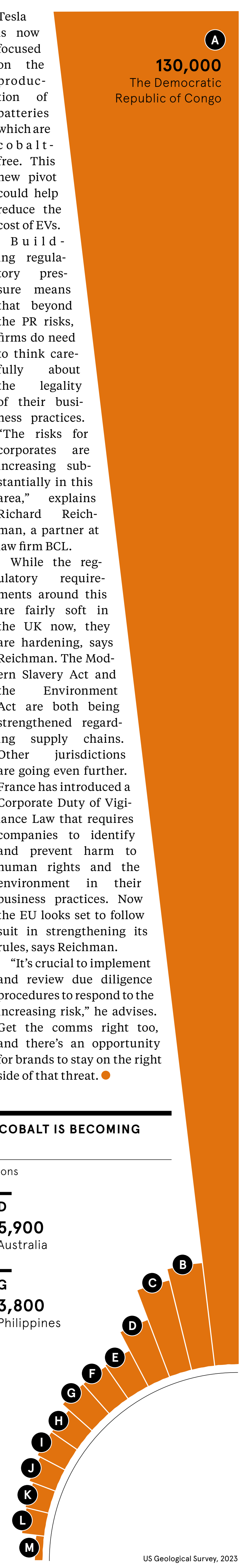
Building regulatory pressure means that beyond the PR risks, firms do need to think carefully about the legality of their business practices. "The risks for corporates are increasing substantially in this area," explains Richard Reichman, a partner at law firm BCL.

While the regulatory requirements around this are fairly soft in the UK now, they are hardening, says Reichman. The Modern Slavery Act and the Environment Act are both being strengthened regarding supply chains. Other jurisdictions are going even further. France has introduced a Corporate Duty of Vigilance Law that requires companies to identify and prevent harm to human rights and the environment in their business practices. Now the EU looks set to follow suit in strengthening its rules, says Reichman.

"It's crucial to implement and review due diligence procedures to respond to the increasing risk," he advises. Get the comms right too, and there's an opportunity for brands to stay on the right side of that threat.

THE WEST'S RELIANCE ON CONGOLESE COBALT IS BECOMING A REPUTATIONAL HEADACHE

Top countries for cobalt mining in 2022, in metric tons



B 10,000 Indonesia	C 8,900 Russia	D 5,900 Australia
E 3,900 Canada	F 3,800 Cuba	G 3,800 Philippines
H 3,000 Madagascar	I 3,000 Papua New Guinea	
J 2,700 Turkey	K 2,300 Morocco	
L 2,200 China	M 800 US	

US Geological Survey, 2023

Commercial feature

The hidden opportunity in recovering VAT

Businesses suffering due to rising costs and supply chain issues are often too busy to spend time clawing back VAT refunds from international transactions. But getting back these funds does not need to be costly or time-consuming

For any firm with a sales presence in multiple territories, keeping on top of receipts and invoices can be a near constant task. Software giant Citrix, which operates in APAC, EMEA and Japan, among other jurisdictions, employs a designated accounts payable department, as well as the latest travel and expenses monitoring assistance. However, in a fast-moving business, manually selecting and chasing VAT refunds across international transactions became increasingly difficult, says Judith D'Aguilar, global VAT director at the company.

"We had a whole accounts payable department looking at manual expenses, choosing the invoices they thought were reclaimable and processing the expenses in a very manual way," she says. "We had complaints because it took a long time for payments to be made to employees, who had to go back and get receipts where there were none. Sometimes AP staff didn't know how to categorise expenses; that manual process is prone to errors and delays."

With these friction points, Citrix suspected that VAT refunds were slipping through the cracks. The company onboarded VAT IT to simplify processes and optimise recovery, only paying the firm a fee if funds were recovered.

In the first year, VAT IT recovered $900,000 (£750,000) for Citrix. "We can now say we are maximising our reclaim for all these entities. We can also see what is being incurred from an expense perspective, as well as what is recovered and what is in the pipeline."

VAT IT specialises in identifying and reclaiming tax refund opportunities for international businesses using a mix of human and technological expertise. Operating like a VAT bounty hunter, the firm, which has 23 years of experience, only charges if it manages to recover money.

VAT IT has pulled back as much as £10m in a single year for a client. Yet the number of international businesses, both large and small, leaving cash on the table is growing in a rapidly changing global climate, says Marc Sevitz, managing director for global operations and enterprise at VAT IT.

"Citrix is a great example. As a successful global software business, it has sales teams moving between countries who stay in hotels and have travel expenditure that we recover VAT on," he says.

"Smaller businesses are also missing important returns. If a firm gets back £200,000, that can make or break the business. In staffing costs, that £200,000 could mean five or six decent hires. How many sales or manufacturing staff is that, that could then help grow the business? That's a whole evolution it might have left behind."

International businesses have faced significant upheaval in recent years due to the pandemic, Brexit and the war in Ukraine. This has often forced them to switch supply chains and be exposed to new territories and jurisdictions. This means many firms are not aware of the refunds they are leaving unclaimed, says Sevitz.

"Brexit laws were such that it made it harder to recover VAT. The previous EU process was more digital, now the post-Brexit UK is much more manual. Saying to a business they have to do more paperwork forces extra time and extra mistakes. We see that in the money we reclaim for businesses," he adds.

Lockdown also forced people to work from home and while businesses have invested in new technology, many have cut costs in the subsequent economic downturn, says Sevitz. "Often one of the first things to go is finance teams. Businesses say they are going to do VAT internally and remotely across departments, yet none of whom are working in one office. That's where mistakes get made."

> The number of international businesses, both large and small, leaving cash on the table is growing rapidly

VAT refunds can be uncovered in the most unusual of places. For instance, pharmaceutical companies often find themselves using millions of test tubes each one produced in two different territories: the glass vials in one jurisdiction and plastic tops in another. A single fashion item may have buttons, cotton or zips produced in multiple places. This can mean VAT costs incurred at different points have to be claimed back.

Few firms are more vulnerable to this than a soft drink firm that sells 500 million bottles and cans across 28 countries. Before the firm partnered with VAT IT in 2018, not only did it need to claw back money from across varying territories and products, it also needed to marry up any VAT analysis with an expense management process that was complicated and dependent on inflexible technology.

The international firm was able to simultaneously sync its existing technology with VAT IT's 'VAT Cloud', a cloud-based platform that has real-time reporting capabilities.

"VAT Cloud easily extracts expense data from Chrome River and automates, centralises and enhances the company's VAT recovery and compliance," says a spokesperson from the company. "Refunds go straight back into the business, boosting cash flow for future investment. It is easy to standardise and centralise VAT compliance when we originally thought it was a heavily localised function. Best of all is that VAT Cloud is easily accessible to our global VAT teams."

The VAT Cloud client interactive portal allows businesses to have a continuous up to date view of their VAT claims process, what refunds are successful, and what is happening with each invoice and expense. This visibility gives critical insight into funding.

Alongside this technology, VAT IT has a strong human element, says Sevitz. "We are not just paper peddlers, we do not just take a firm's invoices and give them to a VAT authority, we understand the process from end-to-end and know what to ask for. We have a team of 50 legal experts who work solely on understanding whether complex transactions have a VAT recovery opportunity and if there are queries from the tax office we answer those as well."

Whether a business currently puts all its invoices and expenses in a drawer or a box, or uses an up-to-date digital expense management system, VAT IT can seamlessly collect them and immediately get to work, bringing value back into the business.

As D'Aguilar at Citrix says: "VAT IT has led us right. It has recovered for us and we've never had an audit because the firm reclaimed something it shouldn't have. The company understands the rules, we trust them; it's a win-win."