

Fung Group Supplier Code of Conduct Update

Update
Sept 2019

Content

Why Compliance Matters

Compliance Program Updates

Why Compliance Matters

Our Commitment

“We aim to develop and operate **responsible, sustainable**, agile supply chains that meet the demands of a dynamic global retail sector and address our common, global sustainability challenges.”

Group Chairman, William Fung, 2018 Annual Report

Why Compliance Matters



TRANSPARENCY

The number of major fashion brands disclosing first-tier supplier lists increased 2X from 2017

More pressure on brands to monitor deeper in the supply chain and to publish factory performance

ENVIRONMENTAL FOOTPRINT

Paris Climate Agreement, China Environmental Law, EU Directive on Plastics, EU Circular Economy Act, Audit Committee Rec. In 2019, Fung Group signed a Fashion Pact, committing to improving sustainability standards. Environmental inspections and follow up visits to continue in China in line with regulatory updates.

Industry and Li Fung's customers keep making more commitments to fight environmental crisis.

SOCIAL AND WORKER WELL BEING

Child Labor (e.g. new Dutch Child Labor Due Diligence); Modern Slavery (new Australia Modern Slavery Act); continued focus on safe workplaces (new industry initiatives)

Why Compliance Matters

- Compliance is the **right thing** to do
- **Compliance** with legal & customers' requirements
- Supply chain risks **management**
- Business, brand & reputation **protection**
- Building **competitive advantage** for customers

Price + Quality + Delivery + **Compliance** = customer's first choice

Why Compliance Matters

Unauthorized Subcontracting: In June 2017, US\$100K penalty was placed on a vendor due to unauthorized subcontracting in China

Child Labor: In September 2018, customer dropped business due to child labor found in a factory in Bangladesh

Clients have fined vendors (US\$500-2500) or held orders for critical compliance violations such as illegal termination, wage withholding, lack of maternity benefits and others. No new orders are allowed before remediation completion.

China Environmental Inspections 2018

- 25,000+ people from industry and government disciplined
- 29,000+ enterprises fined for over US\$ 350 million in total
- 80,000+ factories shut down

How to Ensure Compliance

- Review changes in updated Supplier CoC
- Understand and be clear on processes and procedures for meeting compliance
- Ensure there are **NO** Critical and Zero Tolerance issues among suppliers you work with
- Work closely with suppliers ensuring critical issues are all remediated
- Promote continuous improvements

Encourage Suppliers to take **ownership** over their compliance performance

Our Compliance Program

STANDARD

Supplier Code of Conduct

&

Minimum Compliance Requirements

MONITORING

Comprehensive Audit by 3rd party firms:



Equivalency Program for Industry Alignment

Better Work	BSCI	BV Standard	RBA
SMETA	ICTICARE	RJC	SA8000
FLA SCI	UL RSWA	WCA	WRAP

ASSURANCE

Spot Checks

&

KPIs with 3rd Party Audit Firms

REMEDIATION

- Root Cause Analysis
- Remediation Tracked & Verified by ELEVATE or Specialized Third Parties
- Training & Capacity Building

Industry Partnership & Collaboration

Compliance Program Updates

Background

Supplier Code of Conduct and its related Standards Package are updated every three years to reflect changes in national and international laws and to align with company and customer values and priorities.

The recent update aims to state the company expectations for suppliers in a positive and simple manner and sets out aspirational goals for our suppliers in the form of “best practices”. It also includes the requirement that suppliers ensure LF Standards are respected by next-tier suppliers. The update was done following a comprehensive mapping and review of:

- ❖ Local, national laws/regulations
- ❖ International laws including ILO Conventions
- ❖ Fung Group values
- ❖ Customer values and standards

Key Focus Areas



Safe Workplace



Respect Fundamental Rights



Transparency and Ethics



Environmental Resilience

 LI & FUNG

Supplier Code of Conduct

January 2020

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Key Focus Areas



Safe Workplaces

- Responsible fire safety and emergency precautions and practices
- Responsible policies and practices on first aid and occupational safety and health
- Safe and clean dormitory, child care and canteen facilities
- Responsible chemicals and hazardous materials, special equipment and spaces safety management
- Responsible electrical, building and construction permits, policies and practices



Respect Fundamental Rights

- All work is freely chosen
- All workers meet minimum age requirements (15 or legal age in country, whichever is higher)
- Treat all workers with respect and ensure equality of treatment
- Uphold the right to freedom of association and collective bargaining
- Responsible hiring, wages, benefits, working hours and termination practices
- Functioning grievance mechanisms

Key Focus Areas



Environmental Resilience

- Establish and implement an environmental management system
- Minimize impacts of chemicals, wastewater, air emission, waste and noise pollution
- Improve energy and resource efficiency



Business Transparency and Ethics

- Suppliers are transparent and engage in continuous improvement
- Suppliers engage in ethical business practices
- Subcontracting and homeworking are authorized with prior written consent
- Business licenses meet or exceed legal requirements

Key Updates

1. More robust coverage on all forms of modern slavery and child labor, with clear provisions on responsible recruitment (in accordance with the AAFA commitments) and hazardous work for young workers.
2. Strengthened focus on the environment including one new D-rating on illegal discharge posing immediate threat or serious damage to the environment
3. Enhanced guidance related to bribery and unauthorized subcontracting (more detailed description and definitions to prevent misunderstanding)
4. Update on F-ratings
 - Aligned with customers and new ILO Convention on Violence in the Workplace by including reference to severe psychological abuse along with physical abuse
 - Added one new F-ratings on gross or repeated negligence causing serious injury or death
5. Updated Supplier Code of Conduct effective as of 1st January, 2020

Robust Coverage of Modern Slavery & Child Labor

- Additional requirements on **responsible sourcing** practices, ensuring suppliers do not purchase raw materials from regions or countries with systemic forced labor or conflict minerals
- **Responsible recruitment:** ensuring workers do not pay for their job; retain control of their travel documents and have full freedom of movement; and are informed of the basic terms of employment before leaving home.
- Suppliers shall ensure working conditions of employees under the age of 18 follow the law and do not jeopardize the health, safety or morals of the employees.
- Suppliers shall **remediate** all cases of child labor in the best interests of the child. Costs of child labor remediation, including those identified in next-tier suppliers or contractors are charged to the supplier.

Responsible Recruitment

Employees shall be free from paying recruitment fees or related costs. Where recruitment fees or related costs are charged this must be covered by the employer. Indirect fee charging (such as through deductions from wages and benefits) is prohibited. Suppliers must ensure that where employees have paid recruitment fees, fees are reimbursed by the employer within a reasonable period of time.

Recruitment fees include:

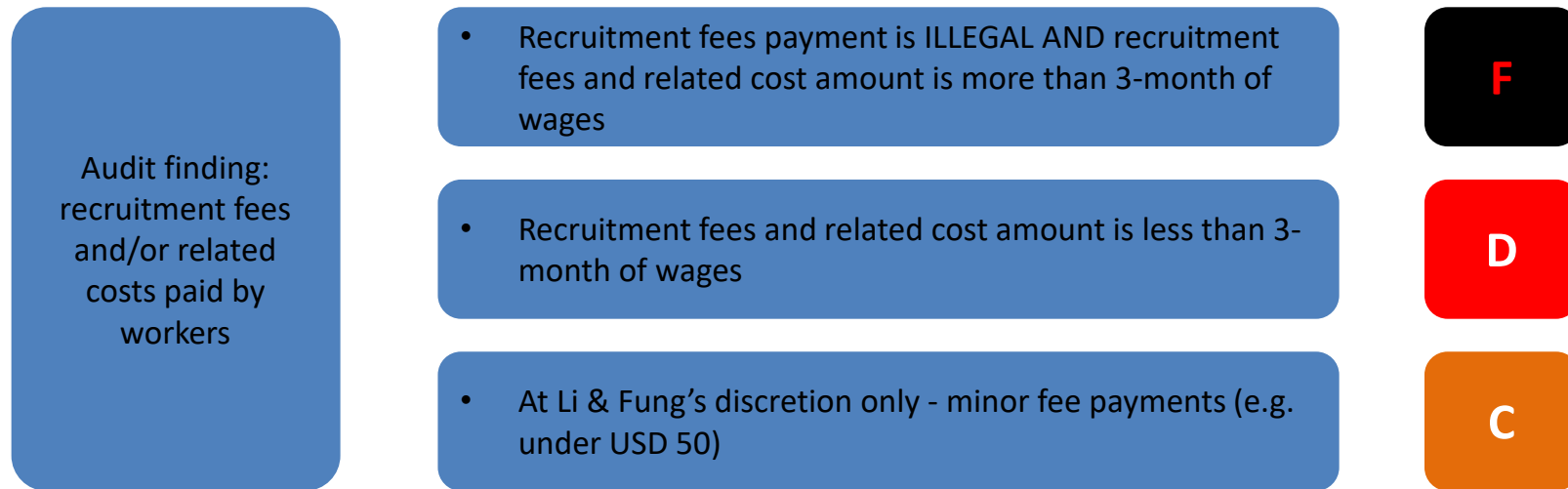
- Payments for recruitment services offered by labor recruiters
- Payments made in the case of recruitment of workers with a view to employing them to perform work for a third party;
- Payments made in the case of direct recruitment by the employer; or
- Payments required to recover recruitment fees from workers

Cost initiated by an employer / recruiter / agent:

- Medicals cost
- Insurance cost
- Cost of skills and qualification test (incl. language)
- Cost of training and orientation
- Equipment cost (incl. uniform)
- Travel and lodging cost

Responsible Recruitment

Depending on the amount of fees paid by the workers and whether the fees paid are legal in the country of origin and destination different compliance rating will be assigned for the audit findings:



Note: Within the first year of implementation (2020) Li & Fung retains discretion not to apply the rating penalties provided factories reimburse workers within a reasonable period of time. Factories who proactively identify worker payment of recruitment fees and related costs and reimburse them will not be penalized by Li & Fung.

Child Labor

Li & Fung's Code of Conduct prohibits the employment of juveniles no younger than 15 years of age, or younger than the age of completion of compulsory education, or legal employment age of the relevant country (whichever is higher).

When a case of child labor is identified at a factory, there are two flows of remediation, which must be initiated:

- Remediation of the Child: Li & Fung has signed an MOU with the Centre for Child Rights and CSR (CCR CSR) to provide services for child labor remediation.
- Remediation of the child has two steps:
 1. Rapid investigation and safe removal of the child.
 2. Education/vocational training plan for the child.

Remediation of the child is extremely time-sensitive and mandatory, regardless of whether the BU will continue with a factory.

Remediation of the Factory: The factory must do a root-cause analysis and take steps to prevent future child labor. Factory CAP management is managed by LF.VATE.

Stronger Focus on Environmental Protection

- Suppliers shall implement an Environmental Management System (EMS) with personnel responsible for monitoring, tracking and improving performance.
- Chemicals: Suppliers shall maintain a list of all chemicals used in the factory and assign personnel responsible for chemicals.
- Waste: Suppliers shall conduct routine monitoring of wastewater discharge and sludge and shall segregate and track waste. Suppliers shall **not** directly discharge wastewater and hazardous waste into the environment or expose hazardous waste to rain or surface run-off.
- Energy and Resource Efficiency: Suppliers must comply with national policies and regulations and have personnel responsible for tracking major consumption patterns of key resources. As a best practice suppliers should use technology to track consumption patterns and set targets to reduce consumption.

Enhanced Guidance on Bribery

Definition: Bribery is when a person offers, promises or gives another person a benefit directly or indirectly (e.g. through a third party) intending that benefit to influence that person to perform their job improperly, or as a reward for doing so. Benefit is not limited to cash or cash equivalent items (such as gift vouchers) and benefit includes any type of advantage.

Examples of bribery (non-exhaustive) include:

- Payment to quality control staff to clear goods for shipment to the customer
- Offering or providing gifts to company staff, its customers or representatives (including auditors) even where it is a locally acceptable practice.

Enhanced Guidance on Unauthorized Subcontracting

Current

All subcontracting and homework activities must be disclosed and factory must maintain written authorization from Li & Fung and/or its customers.

- Suppliers shall inform Li & Fung of all homework and subcontracting activities, regardless of whether these activities are related to the production or service for Li & Fung.
- All homework and subcontracting shall be documented, disclosed, and monitored by the Supplier.

Update

All Subcontracting and Homeworking Activities Must be Disclosed and Authorized.

Suppliers must not use unauthorized subcontracting or homeworkers:

- All subcontractors and/or homeworkers involved with key production processes must be disclosed and receive written approval from Li & Fung and its customers prior to outsourcing production.
- Suppliers are responsible for ensuring next-tier suppliers comply with this Code by performing periodic assessments and training. Assessments shall be performed at a minimum on an annual basis and records kept available for review.
- This section only relates to goods or services produced for Li & Fung or its customers.

Disclosure and Authorization: Suppliers should request to register their subcontractors involved with key production processes or service in LF system and obtain a valid approval period through either a Equivalency Audit Report or Li & Fung Audit.

Physical & Psychological Abuse

Severe and repeated forms of psychological abuse are now an F-rating under LF Code of Conduct. Less severe and/or one-off situations of verbal abuse are a D-rating.

The way we distinguish between different forms of workplace violence depends on the following indicators

- Intent: the actions or words are intended to cause harm to the victims
- Impact: the more severe the impact on the victim the higher chance it should be F-rated.
- Unrealistic demands and abuse of vulnerability: The more unreasonable the demands linked to the abuse the higher than the chance that the words being said are at the extreme end of abusive. Consider if the perpetrator is abusing a position of power.
- Frequency: If the psychological abuse is repeated there is a higher chance it will be F-rated

Zero Tolerance Violations Update

ZT code	Description	Changes
ZC101	Attempted/ committed bribery	
ZC102	Equivalency report falsification	Description: Critical issues related to audit falsification
ZR101	Full access denied	Description: Full access denied or denial of serious accident investigation
ZR102	Unauthorized subcontracting	
ZR103	Unauthorized home working	
ZA101	Underage labor (15 or legal age in country, whichever is higher)	
1 ZF101	Physical abuse/corporal punishment	Description: Worst Forms of Workplace Violence (physical and Phycological abuse) to align with ILO convention
ZF102	Sexual harassment	
ZG102	Lack of business license	
2 ZV101	Involuntary labor: Forced overtime with extreme threat, coercion or penalty	Integrate 5 codes of different forms of forced labor into ZV103 Forced Labor
ZV102	Involuntary labor: Prison labor	
ZV103	Involuntary labor: Bonded or indentured labor	
ZV104	Involuntary labor: Use of trafficked humans or slavery for labor	
ZV105	Withholding employees' original identification documents (ID)	
ZV106	Withholding deposit as a condition of employment	Description: Debt-bondage: payment of illegal and excessive recruitment fees
ZW101	Non-payment of wages more than 2 pay periods	
3 ZE101	Evidence of potential structural collapse risk	Description: High-risk of immediate structural collapse
ZE201	Gross or Repeated negligence (e.g. management system and implementation of H&S) leading to loss of life or serious accident	New code. The gross or repeated negligence are common from incidents, adding such code will enable incident to have better tracking records as well as remediation follow up.
4 ZE102	Locked or systematically obstructed emergency exit	
ZE103	Bangladesh factory failed to complete 100% Accord/Alliance remediation	Removed. Factory failed to meet the remediation requirement will be simply deactivated until the remediation completes

Updated Zero Tolerance by Themes

Zero Tolerance (F)

Safe Workplaces

- High risk of immediate structural collapse
- Locked or systematically obstructed emergency exit
- Gross or repeated negligence leading to loss of life or serious accident

Transparency and Ethics

- Attempted or committed bribery
- Critical issues related to audit falsification
- Full access denied or denial of serious accident investigation
- Unauthorized subcontracting*
- Unauthorized home working
- Lack of business license

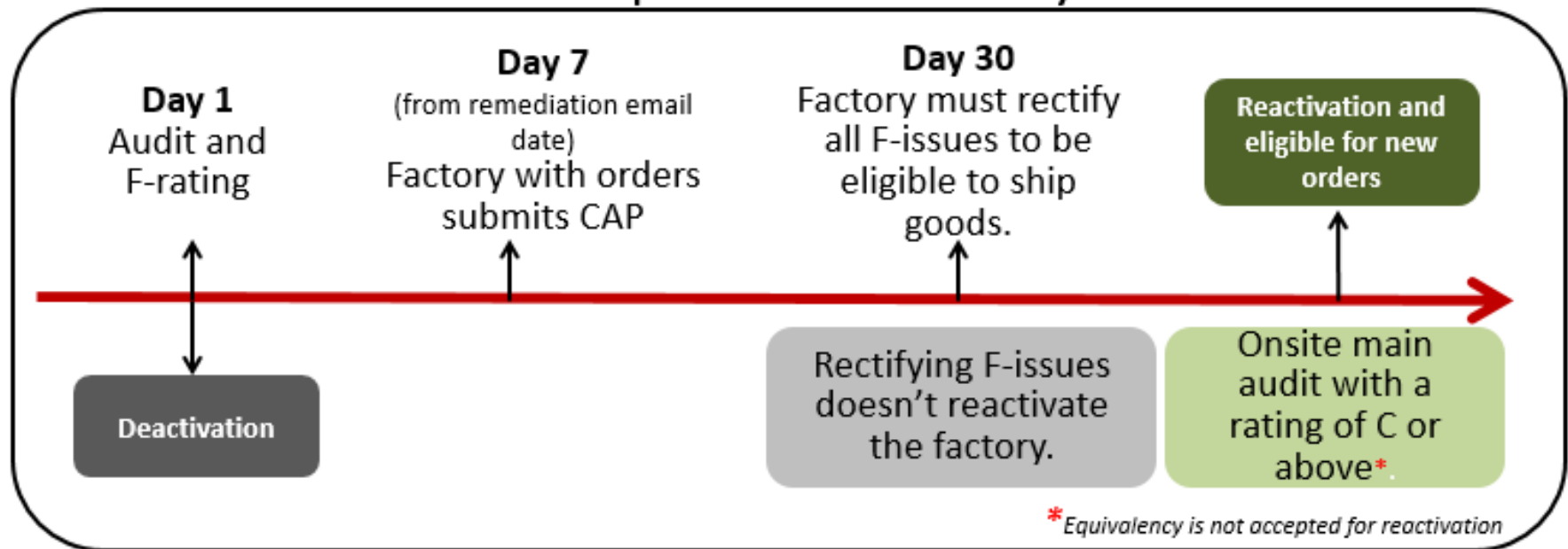
Respect Fundamental Rights

- Underage labor (15 or legal age in country, whichever is higher)
- Worst forms of workplace violence (sexual harassment, physical and psychological abuse)
- All forms of Forced labor
- Payment of illegal and excessive recruitment fees and related costs
- Non-payment of wages for more than 2 pay periods

Zero-tolerance issues must be remediated immediately and may result in Suppliers being permanently prohibited from producing merchandise for Li & Fung and its customer

F Remediation Workflow

Remediation process for F rated factory



** To re-join LF supply base, factory must demonstrate sustainable improvement with a new audit rated C and above **

Updated Critical Violations by Themes

Critical Violations (D)

Safe Workplaces

- Impeded access to emergency exit or pathway
- Inadequate number of emergency exits
- Setting of emergency exit doors obstruct evacuation.
- Critical risks from unsafe electrical conditions
- Lack of electrical grounding
- Combustible or toxic substances stored in residence
- Immediate fire hazards from reckless or negligent behaviors or from the incorrect storage of flammable materials
- Gross negligence from unlicensed people/machines, site hazards, dangerous operation which may or already caused serious disease, or accident.
- Evidence of potential structural collapse risk which needs continuous surveillance

Transparency and Ethics

- Record falsification or conflicting
- Coaching, retaliating, or bribing employee for interview; dismissing or hiding employee to evade audit
- Partial access denied

Environmental Resilience

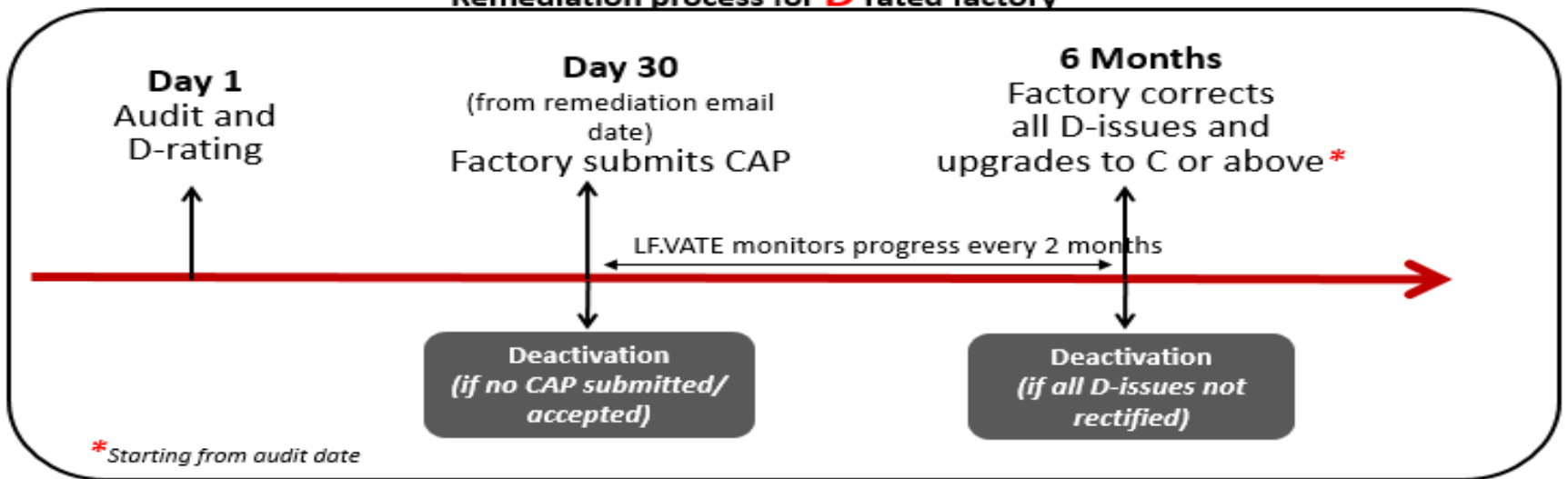
- Illegal discharge poses an immediate threat or serious damage to environment or local communities

Respect for Fundamental Rights

- Unlawful working hour or hazardous conditions for vulnerable categories of workers (pregnant, nursing, young or disabled workers)
- Unlawful rest, benefit, payment arrangement for female workers (pregnant, nursing etc.)
- Illegal termination
- Worst forms of discrimination in hiring or employment (discrimination which causes severe impacts on victim or which is systemic)
- 30 or more consecutive work days
- Insufficient time records (multiple or systematic)
- Acts of anti-union discrimination
- Paying below minimum wage
- Monetary fines, or illegal or excessive disciplinary practices
- Illegal deductions, indirect payment, deposits, charges. Or minor fees paid by migrant workers for the purpose of securing employment.
- Insufficient payroll records (multiple or systematic)
- Non-systemic verbal abuse
- Late payment less than 2 pay periods, or indicators of financial distress

D Remediation Workflow

Remediation process for D rated factory



Audit Rating Table

- ✓ Audit ratings and approval periods are based on the types of non-compliances identified at the factory.
- ✓ Supplier must remediate **ALL violations** according to Li & Fung Standards and Guidance

Ratings and approval periods	Ratings Definitions
A: 24 months	Approaching Compliance
B: 24 months	Improvement Required
C: 12 months	Substantial Improvement Required
D: 6 months (0 months for new factories) <ul style="list-style-type: none"> • No approval for new factories • Factory is required to submit an acceptable corrective action plan (CAP) within 30 calendar days. • Failure to submit an acceptable CAP within 30 calendar days will result in factory deactivation (no new orders will be placed). • Failure to rectify non-compliances within 6 months will result in deactivation. 	Immediate Remediation Required
F: 0 month <ul style="list-style-type: none"> • Factory is deactivated in LF system • Factory with orders in production must submit a remediation plan in 7 calendar days and rectify non-compliances in 30 calendar days to be eligible to ship goods. 	Zero Tolerance

Factory Onboarding & Reactivation Requirements

- To **onboard a new factory, or a factory without any business in the last 24 months** a compliance rating of C or above must be achieved through a main audit or equivalency.
- **A factory fails to complete D or F remediation** will need to go through a main audit only (Equivalency is **NOT Accepted**) with compliance rating of C or above to be re-activated.
- Additional conditions may be applied to Bangladesh factories. Following are the **mandatory requirements for onboarding a factory in Bangladesh-**
 - Factory located in a **Multi- Storied and Multi-Tenant (MSMT)** building is not allowed.
 - 100% Bangladesh factories are **inspected either by Accord/RSC or Alliance/Nirapon.**
 - Factory must reach a **minimum average of 90% verified remediation progress rate on initial findings** of Fire, Electrical and Structural Safety per ACCORD/ RSC/ ALLIANCE/ NIRAPON inspection reports.
 - Factory that is under **suspension or termination from ACCORD/ RSC/ ALLIANCE/ NIRAPON is not allowed.**

Vendor Compliance Team Support

It is important to Li & Fung that all Suppliers understand the Supplier Code, remediation processes and can successfully implement corrective and preventative actions. If you have any question, please contact your local Li & Fung Vendor Compliance team.

Mr. Tarikul Islam – 01730041015 / tarikulislam@lifung.com

Full version of the Updated Supplier Code of Conduct is available here:

https://onefamily.lfapps.net/sites/default/files/lf_codeofconduct_2oct2019.pdf

Effective Date

Updated Supplier CoC effective date:

1st January, 2020

Quiz 1 / 5

Which of the following is true according to CoC's policy on Zero Tolerance (ZT)?

ZT may result in supplier being permanently prohibited from producing merchandise for Li & Fung and its customers

Immediate remediation of ZT violations will prevent factory deactivation

Only if two or more ZT violations are identified will the factory be deactivated

Answer

Quiz 2 / 5

What is the new Critical Violation related to environment resilience?

Absence of one or more legally required environment permits

Illegal discharge poses an immediate threat or serious damage to environment or local communities

Presence of unaddressed supervisory environmental records in IPE database (China specific violation)

Answer

Quiz 3 / 5

Which new Zero Tolerance violation was added to Supplier Code of Conduct?

Gross or repeated negligence leading to loss of life or serious accident

Locked or systematically obstructed emergency exit

Coaching, retaliating, or bribing employee for interview; dismissing or hiding employee to evade audit

Answer

Quiz 4 / 5

What is effective date of the updated Supplier Code of Conduct?

As of release date - on 30th September, 2019

30th November, 2019

As of 1st January, 2020

Answer

Quiz 5 / 5

What is required to reactivate a factory deactivated due to a compliance reason?

A compliance rating of C or above must be achieved through a main audit or equivalency

A compliance rating of C or above must be achieved through a main audit only (equivalency is NOT accepted)

A compliance rating of D from a main audit or equivalency with CAP and commitment to remediate violations within 6 months

Answer

Situational Question 1 / 5

An auditor was inspecting a factory and found two children working on the factory's production line. The children's parents turned out to be workers on that same production line and immediately removed children from the production area when asked by the auditor.

- What would be the audit results for this inspection?
- What are the next steps factory & BU needs to make (if any)?

Situational Question 1 / 5

- **What would be the audit results for this inspection?**

Factory social compliance rating will be F.

- **What are the next steps factory & BU needs to make (if any)?**

The factory must commit to work with a designated 3rd parties to complete remediation, which includes ensuring the child is removed from their place of work and placed in education. The child should receive their wages until they turn legal working age. The factory should undergo a training to improve management system and enhance recruitment practices so to prevent child labor cases in the future.

Situational Question 2 / 5

During a quality check a QA found out that factory A subcontracted a production style to Factory B without seeking prior authorization from LF. The factory owner admitted the case of subcontracting, but said that Factory B was also owned by him and claimed that it shouldn't be counted as unauthorized subcontracting case.

- What would the conclusion be? Is it an unauthorized subcontracting case?
- What are the next steps factory & BU needs to make (if any)?

Situational Question 2 / 5

- **What would be the audit results for this inspection?**

It is an unauthorized subcontracting case as the subcontractor was not approved by LF.

- **What are the next steps factory & BU needs to make (if any)?**

The factory has to disclose and stop all unauthorized subcontracting activities immediately, as well as bring back all the subcontracted materials and goods. Follow up actions will include participation in trainings or e-learnings with focus on integrity. An inspection might take place in the subcontractor to assess compliance level.

Situational Question 3 / 5

During an audit, several foreign migrant workers mentioned to the auditor that prior to starting their work they have paid fees to a recruitment agent in their country of origin. The fee payments covered the agencies fees as well as the cost of the plane ticket. The workers come from a country where it is illegal for recruitment agents to charge recruitment fees and the employer is meant to cover the airfare.

- What does this finding mean and how does it affect social compliance rating?

Situational Question 3 / 5

What does this finding mean and how does it affect social compliance rating?

It depends on the amount paid by the workers and whether the fees paid are legal in the country of origin and destination.

1. For payment of illegal and excessive (more than 3-months of wages) recruitment fees and related costs by workers recruited after Jan 2020 the factory will receive a zero-tolerance finding. Factory cannot receive new orders until remediation steps are complete including reimbursing workers for the cost.
2. For payment of recruitment fees and related costs by workers (less than 3 months) recruited after Jan 2020 Violation will be treated as a D-rating with a 6 month or less approval period. As Li & Fung has committed to a “no-fee charging policy” for workers, even payments which might be considered “legal” can be counted as a violation.

Note: Within the first year of implementation (2020) Li & Fung retains discretion not to apply the rating penalties provided factories reimburse workers within a reasonable period of time. Factories who proactively identify worker payment of recruitment fees and related costs and reimburse them will not penalized by Li & Fung. Li & Fung retains the right to wave violations for very minor fee payments, which do not run the risk of trapping workers into situations of debt-bondage.

Situational Question 4 / 5

Li & Fung requests Elevate (the audit company) to undertake an unannounced audit at a factory.

When an assigned auditor arrived to the factory, the factory manager denied the auditor's access to the factory floor. The management explains she was not aware of the upcoming audit

- What are the possible outcomes of this situation?
- What are the next steps factory & BU needs to make (if any)?

Situational Question 4 / 5

- **What are the possible outcomes of this situation?**

“Access denied” is an F rated violation. The factory’s social compliance rating will become F.

- **What is the right course of actions in case of unannounced audit?**

The factory representatives should inspect an auditor’s work badge and authorization letter from LF. If the papers are in order, the auditor should be allowed to access factory territory and conduct an audit. The Supplier Code of Conduct clearly states that “at the sole discretion of Li & Fung and at a time of Li & Fung’s own choosing, Suppliers may be audited according to these Standards and Guidelines”.

If the factory representatives have doubts, they should contact its agent, LF merchandizers, or contacts stated in the authorization letter to verify the information.

Situational Question 5 / 5

You go into a factory and see a manager yelling at a group of workers to work quicker to meet production targets. The workers are migrant workers and the manager is calling them derogatory names. You do some confidential interviews with the workers and find out that derogatory name calling takes place daily. You review the production targets and see the manager has set impossible targets for the workers to meet. The morale in the factory is extremely low and workers fear going to work. Turnover rates are higher than at neighboring factories.

- How would you classify this situation?

Situational Question 5 / 5

- **How would you classify this situation?**

This is a form of workplace violence and could be considered severe psychological abuse (zero-tolerance).

note: it should be F-rated because the abuse is repeated (daily); workers are vulnerable and the manager is in a position of power; the name-calling impinge on the dignity of the workers and the demands being asked by the manager are impossible to meet; impact on the victims is high.

Thank You