

Auditing Suppliers to Reduce Supply Chain Risks

How to use supplier audits to ensure effective China sourcing

10-29-2009



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Among the biggest risks of outsourcing is ensuring that your supplier delivers according to your requirements. Overseas trading companies can disappear overnight or, after signing a contract with one factory, your goods may end up being produced at an unknown subcontractor. Fortunately, supplier audits can help to mitigate many of these problems. This week, Smart China Sourcing spoke with Mike Bellamy from [PassageMaker](#) on the benefits of supplier audits in reducing risk in your global supply chain.

Smart China Sourcing: What does supplier auditing normally include?

Bellamy: There are fundamentally two types of audits:

- Factory Audits which assess the system used by the factory to control quality and run their business.
- Social Audits to assess supplier compliance with safety and environmental standards.

Smart China Sourcing: How does supplier auditing help companies to reduce risks in supply chain?

Bellamy: When talking about “risk”, there are two main kinds of risk.

- Risk that your factory will not produce the agreed product at the agreed quality, price and lead time.
- Risk that your factory will disappear with your deposit or payment.

A factory audit helps to mitigate both risks because a legitimate manufacturer (as opposed to a broker or trading company) is less likely to disappear when there are problems. In addition, a legitimate manufacturer will have a system to control quality, whereas a broker may be here today, and gone tomorrow.

Smart China Sourcing: According to your experience, what are some typical problems most frequently identified during supplier auditing?

Bellamy: I commonly see two types of problems.

The first type of problem results when the seller is not the actual factory, but instead may be a trading company or other type of agent. These agents usually fight hard to ensure the buyer doesn't do an audit because:

- a) they worry that the buyer will go factory direct to get a lower price
- b) they are aware that they lack an effective quality system and are likely to fail the audit.

So the problem is that sometimes intermediaries don't allow the buyer to conduct an audit. The solution to this is simple – find a new vendor!

The second common problem is the “bait and switch”. Some sellers will have an audit done at one factory, but then produce in another factory which may have lower pricing but a poor QC system and low workplace standards. The best way to avoid this trap is to state clearly in the contract that the factory address audited will be the location of production for the order.

Smart China Sourcing: Are supplier audits necessary for established suppliers, or are they only useful for qualifying new suppliers?

Bellamy: You are right that audits are a critical element in selecting a new supplier. However, due to the rapid changes in company ownership, management, customer bases and product focuses in China, I would recommend performing periodic audits on all suppliers to ensure consistency in the supply chain. Such supplier audits are usually not expensive in China, and there are many inspection companies like [China Quality Focus](#) that can offer specialized supplier/sub-supplier audit , production monitoring and defect sorting service at a reasonable price (mostly involving hundreds and not thousands of USD). So audits are an affordable tool.

Smart China Sourcing: Some companies may prefer to have their own on site monitors at supplier locations. Is this an effective way to ensure supplier performance?

Bellamy: The degree of monitoring that you need depends on the complexity of your requirements and the volume of your business. If your requirements are fairly straight-forward and you only need periodic audits and inspections at the supplier, then it is more more cost-effective to hire a third party service provider. If your orders are very large and or your requirements exceedingly technical, then it may make more sense to have your own auditing team on the ground. But keep in mind that the costs of setting up and managing your own sourcing office in China can be substantial. Therefore, in most cases outsourcing audits and inspections to specialists or using a third-party service provider for vendor coordination will save money while still ensuring reliable production.

Smart China Sourcing: How can buyers determine the effectiveness of third-party supplier auditing programs?

Bellamy: Companies sourcing from China should see the benefits of an auditing program through fewer product defects and lower instances of needing to switch suppliers. Over time, an effective program should deliver positive results that are worth many times the cost of the service.

Smart China Sourcing: Can you give three suggestions for companies seeking the most effective third-party inspection service provider?

Bellamy: Everyone's process is different and there is no governing body to regulate the supplier auditing industry like there are for doctors and lawyers, so you must be very careful in your selection process. In particular, we recommend the following guidelines:

- Get references from existing clients from within your target industry, or as closely related of an industry as possible, for any prospective audit vendors;
- Stick with professional companies and stay away from small service providers that have 20 people or less. It is too easy for them to disappear when they make mistakes.
- A competent and reputable service provider of inspection and audit services will provide a guaranty on their work. If your prospective partner doesn't have a professional service agreement clearly stating their terms, conditions and performance guaranty then find a new service provider.

Mike Bellamy is founder and China Operations Director of PassageMaker, an independent company committed to helping buyers conduct quality inspection and avoid IP infringement in China. Recognized as expert on China sourcing, Mike has been a featured presenter for a number of high profile events including Global Sources Asia Expo HK, Global Sources Dubai, Boat Tech China, Rotary Foundation, the US Chamber of Commerce, and the British Chamber of Commerce. To learn more about Mike and PassageMaker please visit www.PSSchina.com.

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