

IDH Auditing Guidelines **For verifying living wage gaps**

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Introduction

Living wage projects, led by diverse groups of partners and stakeholders, are taking place all over the world. As focus on this important topic has continued to grow, so too has the need for uniformity around how living wage gaps are calculated. Consistent and aligned living wage gap analysis is crucial to the effectiveness and credibility of strategies to close gaps and achieve decent standards of living for workers.

For buyers or traders that have supply chain partners all around the globe, alignment around both the living wage concept and how living wage gaps are measured is fundamental to building trust and the capacity to scale up. For producers and manufacturers that are asked to calculate the living wage gap at their production level, uniformity will ensure clarity and reduce inefficiencies. An independent confirmation that the living wage gap has been calculated correctly provides the basis of trust for a dialogue between supplier and buyer on how to close the living wage gap.

For this purpose, IDH developed The IDH Base Report: a report that will serve as the physical evidence that the living wage gap has been calculated correctly. The IDH Base Report can be delivered by third-, second- or first party schemes, as long as the auditors are trained and passed the exams. These auditing guidelines are created to give clarity to first-, second-, and third-party auditing bodies and/or schemes and their auditors.

Introduction to the guidelines

This document is divided into five sections to guide the auditor through the process of a living wage gap auditing.

- Section 1: General instructions (standalone- versus integrated auditing)
- Section 2: Guidelines for preparation of a Salary Matrix audit
- Section 3: Guidelines for conducting an on-site Salary Matrix audit
- Section 4: Guidelines for closure post a Salary Matrix audit
- Section 5: Annexes for specific auditing instructions per sector (primary production, manufacturing, etc.)

Scope of the IDH guidelines on auditing for living wage gap verification

These guidelines are intended for auditors that perform on-site audits of Salary Matrix wage data as part of the verification of living wage gaps. They are designed to have a uniform approach to the on-site audit. The delivery includes the completion of the *IDH Base Report for auditors involved in verifying living wage gaps*, which is expected to:

- focus on the proper entry of accurate data into the Salary Matrix (or an IDH recognized equivalent tool).
- be performed only by auditors who have been trained by an IDH recognized trainer and successfully passed their exam and received their auditor identification number (auditors will need to identify themselves in the IDH Base Report with the number they received after their exam).
- only be done if the living wage gap calculation performed by the company is not older than 6 months to enable effective worker confirmation of the remuneration that they received.
- be used for **on-site** audits only, because interviews with workers are essential. Hybrid or desk-based audit processes can only be used as an add-on but it cannot replace the on-site audits.

In the audit process on-site, auditors can come across cases where an IDH pre-audit desk-based check has been conducted. During such a check, a consultant remotely provides recommendations on how to make a Salary Matrix according to user guidance and national legislation. The result can support the auditor on their on-site audit.

The Auditing Guidelines in combination with an existing scheme

The Auditing Guidelines have been created for schemes, first¹-party, second-party² and for third-party³, that want to include the Salary Matrix audits as part of their living wage requirements and verification processes. Although the intent of each type of audit is the same when executed on-site, the instructions for auditors are influenced by the type of audit (first-, second- or third party) and therefore different from third-party auditing that has extensive governance models.

First- and second-party auditing

These auditing guidelines describe the process for first- and second-party auditors that work directly for companies or are hired by companies to audit on their behalf. It provides the framework for first- and second-party audits that either execute a stand-alone verification of the living wage gap or integrate this audit into the broader scope of social compliance issues that are part of the first- and second-party scheme. These auditing guidelines have to be respected when executed on-site in combination with a first- and/or second-party scheme. In case of questions or need of back-up/support, the auditor should contact IDH.

Third-party auditing

These auditing guidelines describe the auditing process for third-party auditors that work for third-party schemes and audit against an existing sustainability standard. It provides the framework for third-party schemes that either purely focus on the verification of the living wage gap alone, or integrate this auditing into the broader scope of sustainability criteria in their scheme. It supplements and supports the scheme's own audit and verification protocol as it pertains to matters of worker wage assessment and verification. In doing so, the Salary Matrix audit is meant to be undertaken as an add-on or as integrated into ongoing business-as-usual audits that the scheme and their auditing bodies would undertake regularly.

If the scheme does have detailed protocols that guide auditing bodies and auditors on how to assess and audit wage and wage gaps, then it is the scheme's protocols that take precedence. For e.g.: sample size for determining number of worker interviews that auditors must undertake. The auditing guidelines and IDH Base Report provide also the minimum worker interviews per element in case the scheme does not have a sample size exercise.

If the scheme does not have detailed protocols in place to guide CABs or its auditors then it will rely on these auditing guidelines. In such cases, the adoption of these guidelines, along with the IDH Base Report, is sufficient to report audit results.

¹ **First-party audit:** refers to an audit executed under supervision and against the criteria set by an individual company and conducted by internal auditors.

² **Second-party audit:** refers to an audit executed under the supervision and against the criteria set by an individual company and conducted by contracted, external auditors.

³ **Third-party audit:** refers to an audit executed under the supervision and against the criteria set by an independent certification or verification scheme and conducted by trained and specialized auditors.

Audit time and costs

Pilots have shown that a stand-alone on-site audit of living wage gaps requires approximately two days and includes preparation, document review, on-site auditing and delivering an IDH Base Report. With effective preparation, the Salary Matrix audits could be effectively done within a day. However, when the Salary Matrix gets integrated into existing sustainability schemes, it will become part of the existing audit cycles where auditors audit against the full scope of requirements of the standard. In such a scenario, a few hours may be enough as an auditor checks several elements as part of the audit already.

Dealing with sample size when combined with an existing scheme

The calculation of a living wage gap and therefore, the verification of the living wage gap is bound to a unique location. Only in unique situations (please see paragraph 3.3) can several locations be combined in one IDH Base Report. An auditing of Salary Matrix data can be combined with existing sustainability schemes. Some schemes work with multi-site options and perform their on-site audits on the basis of sampling a few sites within that group. In case the Salary Matrix audit is done under such a multi-site construction the scheme shall make the link from the audited location to the multi-site certification holder in the IDH Base Report of the individual locations.



Section 1

General instructions

1. General guidance

Next to the instructions provided in sections 2, 3 and 4 explaining the audit process and set of criteria, there are some additional elements to guide the auditor through the audit:

- In the guidelines, references have been added to the [e-learning website](#) of IDH, that has been developed to support producers in the process of filling in the Salary Matrix. The [e-learning website](#) contains helpful information and guidance on each of the elements that the auditor will check for accuracy and completeness during the audit and therefore when elements are unclear, the e-learning website may provide direct support. It is therefore recommended to have access to the [e-learning website](#) during the audit.
- The IDH Auditing Guidelines are based on the Anker & Anker methodology. Their methodology and benchmark reports are currently seen as the gold standard for estimating living wages for a particular place. In their book '[Living Wages Around the World](#)', the Ankers explain the methodology, which includes core principles of a decent standard of living drawn from widely accepted international agreements and standards. The Salary Matrix, and therefore the auditing guidelines, were developed in alignment with these principles, thus enabling one-to-one comparison with living wage benchmarks. '[Living Wages Around the World](#)' can be downloaded for free. It may help auditors better understand the logic behind the auditing process.
- The definition of living wage is: '*The remuneration received for a standard workweek by a worker in a particular place sufficient to afford a decent standard of living for the worker and her or his family. Elements of a decent standard of living include food, water, housing, education, health care, transportation, clothing, and other essential needs including provision for unexpected events.*' Because food, water, housing, education, health care, transportation, clothing and other essential needs, including a provision for unexpected events, are declared as basic human rights, remuneration can only be accepted according to this definition when it lowers the costs for any of these basic human rights. This principle should always be taken into account during a living wage audit.
- Furthermore, there is a list of principles that any element of remuneration (wages, bonuses or in-kind benefits) must comply with. All of the principles have to be met in order to be counted in the Salary Matrix and verified as accurate by the auditor on-site. The principles are listed beneath and further explained in the 'Take-home document' which is provided after the training on living wage. Remuneration can be counted towards a living wage when it is:
 - Expected by workers and more or less guaranteed;
 - Received within a year;
 - Earned within a standard workweek, not to exceed 48 hours.
 - In-kind benefits must be considered of benefit and value to workers or their families and for personal use;
 - In-kind benefits must be additional to what is freely available through public systems and be included in the cost of living as outlined in living wage benchmarks;
 - In-kind benefits meet international standards of decency;
 - In-kind benefits should not interfere with workers and families rights of self-determination.

Section 2

**Guidelines for preparation
in advance of a Salary
Matrix audit**

2. Guidelines for preparation

It is recommended for auditors to prepare to guarantee a smooth and efficient audit by collecting and reviewing the below information:

- Relevant local and contextual information
- Legal minimum wage for the location being checked
- Valid bargaining agreements (CBAs) for the sectors or industry (where applicable)
- The tax situation to make sure the gross values are taking that into account
- A copy of the relevant living wage benchmark
- A map of the facility and nearest towns where workers live
- A seasonal calendar or reference materials on seasonality of the production (and possible worker migration)
- A copy of the Salary Matrix (draft report or draft excel)
- (Number of) Locations of all sites when a facility has multiple locations or is part of a multi-site/group (to determine the number of visits through a sample size exercise)

Furthermore, the auditor may request already some information and documents or request the auditee to have it available during the audit:

- Excel file of the submitted Salary Matrix
- Payroll records
- Employer's portion of pay slips
- Policy on bonuses
- Records on bonus disbursements
- Piece-rates for all job categories that pay workers by piece
- Records on total pieces completed in the reference year and total units sold
- Policies on in-kind benefits
- Description of methods used to calculate in-kind benefit "costs to employer"
- Cost receipts for in-kind benefits
- Description of childcare benefits (if not provided in the Salary Matrix)
- Any other human resource records that the facility thinks would be useful
- Example of employment contracts
- CBA or a similar document which will give much more context information for the auditor to evaluate if payment breakdown is actually meeting 'legal' requirement
- Example of a timesheet/time record (time in, time out) that would provide a clearer picture of the payment scheme.
- Efficiency scheme documentation

Section 3

Guidelines for conducting an on-site Salary Matrix audit

3. Guidelines during the audit

During the living wage audit, the auditor checks the completeness and accuracy of the Salary Matrix data and its analysis to verify the accuracy of living wage gap estimate. The Salary Matrix completeness exercise is a difficult process for which the IDH Audit Guidelines and IDH Base Report have been created to guide the auditor through all the elements of the Salary Matrix. These steps are described in the IDH Base Report in the same order as the Salary Matrix is designed. The auditing guidelines give additional explanation of the process and criteria in the IDH Base Report.

The IDH Base Report can be used directly during the audit as a checklist.

3.1 General instructions

The following general instructions are important to take into account during the audit. These instructions are also integrated into the criteria described in table 1, matching the steps in the Salary Matrix. Please note that this structure is also used in the IDH Base Report.

- i. When performing the audit, makes sure that a) all reviewed records and data reflect the correct year for which the Salary Matrix was completed, and b) all interviewees also understand the appropriate reference year. (e.g., if a Salary Matrix was completed with data from 2021, and the audit is completed in 2022, the auditor should check records for 2021 and inform interviewees that their responses should be for 2021 rather than the current year).
- ii. Extra time, or overtime, is everything that is more than 48 hours a week. While the Salary Matrix tool aims to capture the real time worked, including extra time, time worked beyond the 48 hours in not counted toward a living wage. In other words, the tool was developed on the principle that workers should be able to achieve a living wage within a 48-hour period or less. Therefore, in order for the Salary Matrix to work properly, companies must track numbers of hours worked. Without those values, the tool will not serve its purpose. Auditors must check that the values entered in the tool come from real records of hour worked and are not based on theoretical work schedules, and cross check these during the interviews.
- iii. The workforce context tab in the Salary Matrix provides information about the workforce of a facility. More specifically, it helps understanding who the most vulnerable workers (and/or job categories) are and who therefore need more attention during an audit.
- iv. Always check with the HR department if there are any workers that were hired via an employment/hiring agency. In the workforce context tab information about the total number of workers hired via an employment/hiring agency is included as well. Crosscheck this via interviews, preferable via a worker and/or union representative. If workers are hired via a hiring agency, check if the company has registered this as a separate work category in the Salary Matrix. Also check if workers hired by an agency were required to pay a fee or portion of their wage for this service. Any amount paid by the employee should be deducted from the wage entered in the Salary Matrix.
- v. When performing interviews to crosscheck the data entered in the Salary Matrix, please focus on the job categories with the lowest paid wages.
- vi. Be sure to always include interviews with temporary workers, including (when relevant) workers that are hired via an employment/hiring agency. Identify the bottom-line fee that they receive and cross-check if this is reflected in the Salary Matrix.

- vii. Auditors must be aware of the legal minimum wage for the location being checked, as well as the valid collective bargaining agreement for the auditee's sector or industry (where applicable) and have an understanding of the local tax situation to make sure the gross values are taken into account. In the payroll section of the Salary Matrix, it is indicated for each job category whether the workers in a job category are covered by a Collective Bargaining Agreement.
- viii. For "In-kind benefits" the auditor can check the Living Wage Benchmark methodology available in the region for reference values on in-kind benefits. For in-kind benefits to be valued as part of total remuneration, the benefits must:
 - o be accepted by the workers as being valuable,
 - o directly reduce the cost of a basic but decent standard of living for a worker and her/his family,
 - o be regularly and reliably provided,
 - o be expected in advance,
 - o be directly provided to workers, rather than through legally mandated employer contributions to state run social services (e.g. employer tax contributions to national healthcare programs would not count).
- ix. Please be aware that in-kind benefits might not be reflected in pay slips, which typically represent cash payments only. If not reflected in pay slips, the auditor should look at other evidence for in-kind benefits.
- x. The requirement for sampling of workers for the interviews are integrated in these guidelines and repeated in the IDH Base Report. The auditor shall make sure that a minimum of 5 interviews with workers shall take place. There must be a sufficient representation of men and women (when relevant), as well as temporary and piece-rate workers. A minimum of 5 interviews should be performed but need to be scaled proportional to the size of the facility/farm if the auditor concludes that a minimum of 5 is not representative and/or does not adhere to sound social auditing protocols in a given circumstance.
- xi. Make sure that interviews are executed in multiple work areas or job categories.
- xii. The values in each job category will be based on the median value for that given job category.
- xiii. When a producer has Salary Matrix data available from previous years, check if there has been any change in ratio of full-time to part-time or seasonal employees by comparing records of previous years with the current records. Also check if average working hours for full-time employees have been altered significantly.

3.2 The role of worker- or union representatives

At the end of the on-site audit, the auditor is required to share the outcome of the Salary Matrix audit with an elected worker representative or union representative. The name and signature of the consulted representative with whom the outcome is shared with will be on the front page of the IDH Base Report. If this requirement can somehow not be met and/or the trade union could not be consulted, the auditor must provide arguments why.

3.3 Dealing with multiple locations

A Salary Matrix is in principle filled in for a unique facility and the workers within that facility. However, if a facility has multiple locations or is part of a multi-site/group, the audit on the ground will follow the sampling protocol and sample size of the third-party auditing body for visiting the unique facilities/sites. On those sampled sites, the auditor will verify the filled in Salary Matrix and verify the calculations of the living wage gap. Each unique facility that is visited will have its own IDH Base Report.

Companies that have a centralized payroll system, and have used the Salary Matrix for multiple facilities/sites, may have their living wage gap information checked by the auditor in one IDH Base Report only if:

- The company can prove that the following variables in the central payroll system, associated with the data requirements in the Salary Matrix, are the same in all the included facilities and sites:
 - o average number of units worked for a given timeframe (no major variances in productivity)
 - o payment rates per units
 - o access to the same bonuses and in-kind benefits
 - o value of the bonus and in-kind benefit
 - o value of gross living wage benchmark for the region where they are located.

If one of the above variables is different, the locations are out of scope and cannot be combined in one IDH Base Report.

- In cases where the variables related to the central payroll system are the same for several locations, the auditor always has to visit the sites (based on sampled selection of sites that relate to the schemes sampling size) that are included in one IDH Base Report to interview the workers on-site. The IDH Base Report shall:
 - o list all sites that have been visited and where interviews with workers were performed.

3.4 Reporting deviations in the IDH Base Report

During the audit, the auditor might find deviations within the data filled in the Salary Matrix. IDH does not interfere with the classification of deviations within individual schemes, but rather only identifies four types of findings per audit point:

Yes = the data entered in the Salary Matrix is correct

No = the data entered in the Salary Matrix is not correct

Partly = the data entered in the Salary Matrix is partly correct

Not applicable = the element is not applicable

For all the elements where the auditor found 'no', 'partly', or 'not applicable', he/she can give a short justification in the IDH Base Report.

3.5 Instructions of the audit process

This chapter provides guidelines on how an auditor can verify the data points that are required to use the Salary Matrix are entered correctly. For each of the elements in the Salary Matrix, guidance and criteria to be checked are described in these guidelines. The table follows the same structure as the IDH Base Report to ensure the criteria in these guidelines are followed.

For each element, there is a link to the [e-learning website](#) of IDH providing guidance. Furthermore, examples are provided to support the auditor by showing real life practices.

Table 1 Guidance on the audit process

I <u>General information</u>		Guidelines
1	Calendar year of wage data	Please check if the calendar year of wage data reflects the correct year.
2.	Currency	Please check if the local currency is entered in the Salary Matrix correctly and reflects the currency used to pay employees.
3.	Production location	Please cross check the GPS coordinates used by the facility. Here you find a link that can help you: https://www.ubergizmo.com/how-to/read-gps-coordinates/
II <u>Benchmark</u>		

1.	Gross living wage	Check if the wage entered is based on gross living wage where possible (might not be possible for purchased values). The gross living wage estimate is the gross pay required to ensure sufficient net take home pay to cover the cost of a decent standard of living. This is necessary because net living wage would not account for statutory deductions from pay (such as income taxes, social security taxes, and union fees) which will reduce the take home pay and money available for day- to-day expenses.
III <u>Workforce context</u>		Guidelines
1.	Worker organisations	<p>At the end of the audit the outcome is shared with an elected workers representative or union representative. The number of registered trade unions that are active in a facility indicate whether a union representative is available/active.</p> <p>Please check if not by registered trade union, workers are represented by another type of workers organization (e.g. workers' council)</p>
2.	Paid leaves and holidays	Please select relevant job categories with HR and crosscheck with proper evidence if the number of workers is entered correctly in the Salary Matrix.
3.	Number of days of unpaid mandatory leave	Crosscheck at least 1 job category that the number of unpaid mandatory calendar days are correctly entered in the Salary Matrix.
4.	Indirect contracting of workers via 3 rd party	Please crosscheck with payroll records or other documentation to see if the number of workers is entered correctly in the Salary Matrix.