

A Change to Our Approval Process

In 2007, we will make a slight modification to our factory approval process to bring needed flexibility to our product pipeline. All garment factories seeking to produce internally-designed and branded apparel for Gap, Banana Republic and Old Navy will continue to receive initial inspection visits prior to the placement of any production orders. In certain narrowly-defined instances, however, garment factories that have resolved all identified major issues may be granted a one-time, conditional approval to produce a special "rush" or "chase" order, even though the factory may still have a few minor issues to resolve. It is important to note that this conditional approval will be short-term, and the factory will not be able to produce additional orders for any Gap Inc. brands until all remaining issues have been resolved to the satisfaction of the VCO.

The Art and Science of Factory Monitoring

Because there is no single standard in the apparel industry, codes of conduct, frequency and scope of monitoring, and team training all vary widely between companies. As a result, monitoring data also varies widely. In our 2004 Social Responsibility Report, we discussed some of the factors that contribute to these variations, and provided guidance on how to understand our monitoring data. For further information, please see the discussion about the "Art and Science of Factory Monitoring" on our website. [E](#)

Our Team

In 2006, we continued to employ a team of more than 90 people around the world who are dedicated to improving the lives of garment workers. This team, which is truly one of our greatest assets, is wonderfully diverse, representing more than 25 nationalities and speaking as many languages. The majority of team members are Vendor Compliance Officers (VCOs), who are responsible for visiting factories, conducting inspections, documenting violations, and working with garment manufacturers and local stakeholders to improve factory compliance with our standards.

We believe strongly in the effectiveness of our team. [E](#) Linked by a common passion to improve the lives of garment workers, our team members are deeply experienced. Most of our VCOs are SA8000-certified auditors, and more than two-thirds have been with Gap Inc. for three or more years. More information about our team and their day-to-day work can be found in our 2003 and 2004 Social Responsibility Reports and on our website. [E](#)

Our Factory Approval Process

In 2005 and 2006, we again required manufacturers and subcontractors that produce internally-designed and branded apparel for Gap, Banana Republic and Old Navy¹ to pass through our approval process before we placed any orders. This process, which is discussed in detail on our website [E](#) and in our 2003 Social Responsibility Report, can take anywhere from a week to more than a year to complete.

We evaluated slightly more new factories in 2006 than in 2005, but approved a lower percentage for production. Of the 425 new garment factories that we evaluated, we rejected 18 percent, compared with 11 percent in 2005.

While we still face many challenges with our approved factories, we know that our approval process helps screen out the worst garment manufacturers, and has a positive impact on factory compliance levels. As the chart on page 28 shows, the factories that we approved for production prior to 2006 had fewer instances of compliance violations than new factories that had not gone through our process.²

2006 Ongoing Monitoring of Approved Factories

Once a garment factory is approved, we strive to visit it at least once a year. Depending on the specific needs of a factory, we may conduct more visits. In 2006, our VCOs conducted 4,316 inspections in 2,053 garment factories around the world, a decrease of about 122 inspections and 65 factories, respectively, as compared with 2005. Because our factory base was smaller, our frequency of inspections in 2006 remained about the same as in 2005. Approximately seven percent of our inspections in 2006 were conducted by teams of two or more auditors. In addition, our VCOs held 1,498

formal and informal meetings with factory managers, an increase of nearly 500 meetings over 2005. The rising prevalence of these meetings reflects our increased focus on helping factories address the root causes of compliance issues, develop effective corrective action plans and provide worker or management training sessions where needed.

In 2006, we conducted ongoing inspections in 99.4 percent of the garment factories approved for the entire fiscal year, and 93.1 percent of those approved for all or part of the year. This was an increase of approximately 0.7 percent and 4.8 percent, respectively, over 2005.

Evolving Our Monitoring Model

In 2004, we noted that the total number of our factory inspections would continue decreasing over time as we experienced ongoing consolidation of our manufacturing base and redefined our monitoring protocol.³ In 2006, we established a special internal team to examine our monitoring protocol and create a new model to focus our resources more effectively.

This team, which will deliver its final recommendation in 2007, has suggested a modified inspection model to tailor the length of our audits and the number of VCOs involved to the size of each factory and its specific needs. Once this new model is finalized, we intend to pilot it in one or two regions in 2007. Based on the results of the pilot, we hope to implement it globally by the end of the year. Going forward, we believe that this new approach will give us more time and more rigorous data to identify the root causes of compliance issues and partner more effectively with factory management and workers to resolve them.

Factory Performance in 2006

As we have noted in our past Reports, few factories, if any, are in full compliance all of the time. Our goal is to work with factory managers to fix problems where we find them and prevent them from recurring. However, some factories may be unable — or unwilling — to address compliance violations. In such cases, we may have to make the difficult decision to terminate our business relationship. In 2006, we revoked our approval of 23 factories for compliance violations, approximately 1.1 percent of our base. This is a significant decrease from the 62 factories terminated in 2005.

Although factory termination remains an important part of our program, we have increasingly come to view it as a last-resort measure. Our first choice is always to work with factory management to resolve issues, since this is in the best interest of the workers as well as our own business needs. We have learned that when we work more closely with our sourcing colleagues and deliver a clear and consistent message as a company about the need for factories to resolve issues, factory managers are more likely to take our requirements seriously. Although this type of internal, cross-functional partnership takes time and patience, we believe