



WORKER RIGHTS CONSORTIUM

WORKER RIGHTS CONSORTIUM ASSESSMENT
Freetrend (Dean Shoes Co. Ltd.), Shenzhen City, Guangdong, China

**FINDINGS, RECOMMENDATIONS,
AND CURRENT STATUS**
November 10, 2009

Table of Contents

Report of Worker Rights Consortium Factory Assessment at Freetrend (Dean Shoes Co., Ltd.), Shenzhen City, Guangdong, China

A. Introduction

- Findings of Noncompliance
- Remediation

B. Methodology

C. Findings, Recommendations and Current Status

1. Unlawful Termination

- a. Findings
- b. Recommendations
- c. Current Status

2. Unlawful Layoff

- a. Findings
- b. Recommendations
- c. Current Status

A. Introduction

This report details the WRC's findings, recommendations and remedial work in relation to the layoff and termination of workers at the FTB sole manufacturing facility of Dean Shoes, Ltd.'s Freetrend subsidiary in Guangdong, China. The 2,000-worker FTB plant is part of the larger Freetrend factory complex which employs roughly 10,000 employees. Dean Shoes is a Taiwanese company that manufactures, as its name suggests, footwear and footwear components for a number of major U.S. footwear brands.

Freetrend and the FTB facility, sometimes known, by virtue of its product, as "Freetrend Sole," are located in Shenzhen, a city of fourteen million people, which was the site of the first of China's Special Economic Zones. The WRC initiated its response to the dismissals of employees at Freetrend in March 2009, after receiving complaints from some of the terminated workers. Freetrend had been disclosed as a supplier of collegiate licensed products to two U.S. footwear companies, K-Swiss and Crocs. The Freetrend factories in Shenzhen also supply non-collegiate licensed products to a number of other major U.S. footwear firms, including Nike and New Balance.

The WRC's work in addressing the dismissals and layoffs at Freetrend was carried out by the WRC's China Director, including multiple meetings with workers, factory managers, buyer representatives, and local civil society organizations, the delivery of a labor rights training to factory workers, as well as a review of relevant documentation. In particular, remediation of the dismissals required extensive collaboration with the compliance staff of both New Balance – at its headquarters in the United States and in Guangdong – and Freetrend itself. As discussed below, this collaboration yielded significant positive results.

Although the number of workers directly affected by the layoff and dismissals is quite small in relation to the hundreds of thousands of jobs lost in the apparel sector in Guangdong over the past year, this case is significant for several reasons. First, it illustrates the challenges for workers in asserting their rights under China's recently-enacted Labor Contract Law¹ in the midst of the ongoing global economic downturn. Second, it shows the vital importance of the rights provided under this law to workers in situations of layoffs and downsizing. Third, it suggests that with engagement by both the WRC and a responsible buyer that has significant ongoing business relations with factory management, workers' rights under the new law can be successfully vindicated.

1. Findings of Noncompliance

As the sole focus of the WRC's work in relation to this factory was the February 4, 2009

¹ Law of the People's Republic of China on Employment Contracts ("Labor Contract Law") (2008) (unofficial English translation available at: http://www.bjreview.com.cn/document/txt/2007-10/16/content_80896.htm).

dismissals, pursuant to the WRC's investigative protocols, this report should not be taken to state conclusions – whether findings of compliance or of non-compliance – in areas not discussed explicitly in this report.

On the basis of the evidence gathered, the WRC documented the factory's noncompliance with both Chinese law and university and college codes of conduct in the involuntary dismissals and layoff of the affected workers. The WRC's findings in this regard are outlined in detail in this report, but, in short, our conclusion was that the factory had violated Chinese law by involuntarily dismissing the workers without adequate cause and by conducting this lay-off without following the process that the law prescribes in such circumstances.

2. Remediation

After reaching these findings, the WRC contacted both Crocs and K-Swiss, as licensees supplied by the company. The WRC also contacted New Balance, since the dismissal occurred at the FTB facility, whose only external customer is New Balance. The two licensees ended up playing a very limited role in the remediation of the violations identified by the WRC. In response to our communications, K-Swiss executives informed us that their company already had decided, for unrelated reasons, to cease sourcing from Freetrend, and, in any case, had discontinued its collegiate licensing program.²

Managers at Crocs stated that while Freetrend was one of their suppliers, as the dismissals in question took place in a production facility that exclusively supplied New Balance the latter should take the lead in addressing the situation. However, Crocs reported to us that, following receipt of the WRC's communication, it held a compliance seminar with its Chinese suppliers and undertook an overall review of its supplier labor compliance policies. Crocs shared an updated copy with the WRC.³ The WRC appreciates that these measures demonstrate Crocs' own commitment to compliance with university codes of conduct.

As a general matter, however, the policy of the WRC is that when labor rights violations are reported at a supplier of collegiate licensed products, the relevant licensee(s) should take an active role in seeking remedies, regardless of whether the supplier's particular production line or facility where the violations occurred is the one which produces the licensee(s)' goods. In this case, however, it appeared that a non-licensee buyer, New Balance, possessed both far greater influence with Freetrend management over labor practices in the FTB facility, where New Balance is the sole customer, and, not

² K-Swiss also stated that its policy was to require all its supplier factories to comply with the SA8000 standard developed by Social Accountability International (SAI). Although a core element of the SA8000 program is factory certification by SAI-approved third party auditors, Freetrend does not appear to have been certified by SAI as SA8000-compliant. The WRC has queried K-Swiss about this issue but, as yet, has received no response from the company. *See*, email exchange between K-Swiss Vice-President Joe Gabaldon and WRC, Apr. 6, 24, 2009 (copies on file with WRC).

³ *See*, Letter from Crocs General Counsel Erik Rebich to WRC (Jun. 8, 2009); Crocs, *Supplier Compliance Manual* (2009) (copies on file with the WRC).

surprisingly, a more highly-developed labor compliance program at the factory than either of the two licensees.

Therefore, the WRC focused its remedial efforts on collaboration with New Balance and its compliance staff, in what ultimately proved to be a fairly effective approach. To their credit, New Balance compliance staff, both in the U.S. and China, worked consistently and constructively with the WRC over a period of several months, and provided the essential encouragement to Freetrend to adopt the WRC's remedial recommendations.

Moreover, for its part, Freetrend management, albeit with significant delay, eventually did implement these recommendations in a thoroughgoing and cooperative fashion. As a result, all of the involuntarily dismissed employees received back-pay for their lost wages and offers of reinstatement – though only one ultimately returned to the company. In addition, to promote compliance with the labor law in any future lay-offs and dismissals, Freetrend published an article discussing the matter in its company newsletter articulating the law's requirements, and the WRC conducted an on-site seminar for FTB workers on their legal rights in such situations.

B. Methodology

The findings outlined in this report are based on the following sources of evidence:

- Offsite interviews with dismissed FTB workers conducted by WRC partner organizations;
- Group discussions with current workers as part of an onsite worker rights training program conducted by the WRC with the cooperation of Freetrend and New Balance;
- Multiple onsite meetings with compliance staff from Freetrend and New Balance;
- An onsite review of relevant documentation provided by Freetrend and New Balance.

C. Findings, Recommendations and Current Status

The following sections review, as applicable for each area of code compliance, the WRC's findings and recommendations, Freetrend's response, and, the status of remedial measures taken by the company. Except where otherwise indicated, for each area of code compliance:

- Descriptions of the WRC's findings and recommendations are based on the WRC's analysis of: (i) information received by our partner organizations from FTB workers in February 2009, which was communicated by WRC to Crocs, K-Swiss and New Balance in a memorandum sent in March 2009; (ii) a report provided to the WRC in April 2009 by New Balance of an investigation it conducted in response to the WRC's communication; and (iii) follow-up memoranda sent by the WRC to New Balance in May and June 2009.
- Descriptions of Freetrend's responses to these findings and recommendations are based on reports received from and discussions with New Balance concerning this issue from April to September 2009; and direct meetings between WRC

representatives, New Balance compliance staff and Freetrend managers in May and September.

- Descriptions of the current status of remedial measures are based on written communications by Freetrend to workers in May, July, August and September 2009; a September 2009 review of other relevant internal company documents concerning the implementation of the WRC's recommendation; and personal observation by WRC representatives.

1. Improper Termination

Findings

On February 4, 2009, Freetrend terminated roughly forty-five supervisory employees from the FTB facility. In the case of twenty-nine of these employees, they were chosen involuntarily by management for termination. Although, reportedly, the reason for the dismissals was an economically-motivated desire to reduce payroll, the explanation given to each of the affected workers was "your [the employee's] performance." Freetrend did not give the employees any details or proof regarding their performance to justify the termination of their contracts.

The WRC subsequently determined that these terminations were contrary to the provisions of China's 2008 Labor Contract Law, and thus violated both New Balance's code of conduct and those university codes applicable to K-Swiss and Crocs. Under the 2008 Labor Contract Law, which mandates the execution of a labor contract as a condition of employing any worker, the justification provided by Freetrend – "performance" – is not, by itself, an adequate basis for terminating an individual employee.⁴

The Labor Contract Law specifies nine different circumstances under which an employer may terminate its employment contract with a worker. The law provides both that employers may dismiss employees during their probation period for failure "to satisfy the conditions for employment," and can terminate workers thereafter if they are "incompetent and remain[] incompetent after training or adjustment of [their] positions."⁵ It does not, however, permit termination of non-probationary employee solely for performance reasons, unless the employer first provides additional training or accommodation. As a result, the dismissals of the twenty-five employees, none of whom were on probation, or had been offered additional training or accommodation, violated the Labor Contract Law.

As has become increasingly common in China since the passage of the Labor Contract Law, some of the dismissed employees contacted local labor authorities, protesting the factory's failure to provide thirty days pay in lieu of advance notice of dismissal. Such notice pay is required under the labor law when a non-probationary worker is terminated without advance warning on account of uncorrectable incompetence, totally

⁴ See, Labor Contract Law, Articles 39, 40.

⁵ See, id.

incapacitating illness, or an unforeseen change in circumstances that makes continued employment impossible.

After the factory agreed to provide the required notice pay to these twenty-five employees, the labor authorities declared themselves satisfied, and the affected employees signed documents accepting termination. According to the factory, once assured that such a benefit would be provided to them, along with their accrued severance benefits, an additional twenty-one supervisory employees came forward, and tendered their resignations.

Nonetheless, several of the involuntarily terminated employees contacted a partner organization of the WRC with complaints regarding the dismissals themselves, not to mention the process by with they were carried out. The WRC determined that any involuntary dismissals of the first twenty-five employees violated the Labor Contract Law's restrictions on permissible grounds for an employer's unilateral termination of an employment contract. As Chinese labor law indicates that waivers of statutory rights are invalid, as are amendments of employment contracts generally when one party "tak[es] advantage of the other party's difficulties,"⁶ our finding was that this conclusion held regardless of whatever arrangement workers had made with Freetrend and the local labor authorities.

Recommendation and Company Response

On March 15, 2009, the WRC sent a memorandum to Crocs, K-Swiss and New Balance recommending that they should direct the company to reinstate and provide back-pay to all of the employees who had been involuntarily dismissed on February 4, 2009.⁷ Freetrend's initial position was that as the local labor authorities ultimately had given the dismissals their blessing, such measures were unjustified.⁸

From late March through early May, the WRC and New Balance exchanged written memoranda and held a series of phone conversations and face-to-face meetings to discuss the case.⁹ WRC and New Balance arrived at a substantial consensus on the steps the company should take to remedy the dismissals. In mid-May, at the prompting of New Balance, Freetrend sent letters to the twenty-five employees informing them simply that the company was hiring again and asking if they would like to apply. Freetrend took the position, however, that to return to employment with the company, these workers would have to repay the severance and notice pay benefits they had already received.

After substantial discussion, the WRC and New Balance reached an agreement this first communication was inadequate and that additional outreach was necessary in order to

⁶ Id., art. 26.

⁷ Copy on file with WRC.

⁸ See, New Balance, Investigation Report of Labor Contract Dissolution for 46 Employees at Freetrend Sole Factory (FTB) (Mar. 2009) (copy on file with WRC).

⁹ See, e.g., id., and WRC, *supra*, n. 7; also, WRC, Memoranda to New Balance Corporate Compliance Manager Lary Brown (May 28, Jun. 12, 2009); Lary Brown, email to WRC (Jun. 10, 2009) (copies on file at WRC).

make explicit that workers were being offered both reinstatement to their positions and full back-pay. The WRC and New Balance concurred that workers should not be required to first repay severance and notice pay benefits, as this would pose a substantial obstacle to workers' exercise of their right to reinstatement. The parties agreed, instead, that any employees accepting reinstatement would simply accrue any additional severance in the future starting from the date of their return to work.

On July 15, 2009, Freetrend sent a second letter to the twenty-nine of the dismissed employees – the twenty-five recipients of the original letter and five other employees whose 'resignations' New Balance determined were not completely voluntary. This letter made a clear offer of both reinstatement and provision of back-pay -- even if reinstatement was declined. The letter also made clear that workers would not be required to re-pay their severance or notice benefits.

Current Status

Between mid-July and late September, twenty-five of the twenty-nine recipients of the second letter responded. Due to the fact that most had already found new jobs, only one of the former employees took reinstatement. All twenty-five, however, collected back-pay for the period from their dismissal to their receipt of the offer of reinstatement. A total amount of 158,309 RMB (US \$23,188) was paid to the twenty-five workers, with each worker receiving from 5,257 to 8,768 RMB (US \$770-1,280). On September 23, 2009, the WRC reviewed documentation provided by Freetrend and New Balance and confirmed the payments. Four out of the twenty-nine employees did not reply to either communication. In sum, over eighty percent of the affected employees were confirmed to have received offers of reinstatement and payment of back wages.

2. Improper Layoff

Findings

In cases where an employer terminates over twenty workers, or ten percent of the workforce, at once, the Labor Contract Law requires that the employer should consult the workers' trade union representative or the workers in advance.¹⁰ The Labor and Social Security Department of Guangdong Province, which has jurisdiction over Shenzhen City, has issued very detailed regulations applying the Labor Contract Law's prior consultation requirement in cases of lay-off of more than twenty workers.¹¹ These regulations state that factories must inform workers thirty days in advance of such a layoff, present a plan for the layoff, and engage in consultation with workers regarding that plan. Because the factory's workers reported that no such consultation occurred prior to the layoffs at Freetrend, the WRC found that the factory has failed to abide by both national law and local (provincial) regulations.

¹⁰ Labor Contract Law, Art. 41.

¹¹ Guangdong Province Labor and Social Security Department, Instruction on Enterprise Redundancy, Closures, Shutdown and Follow-Up Measures for Workers (2008), available in Chinese at: http://www.gzlss.gov.cn/gzlss_new/view_doc.php?id=2214.

Recommendations

In its original communication to Crocs, K-Swiss and New Balance, the WRC recommended that they require Freetrend to affirm that it accepted and understood its responsibilities regarding advance notice and prior consultation in cases of mass layoffs as articulated under the Labor Contract Law and the Guangdong Province Labor and Social Security Department regulations.¹² In the course of the subsequent dialogue between the WRC and New Balance, the parties agreed that this recommendation would be implemented through two means: (i) the publication of an article in the internal company newspaper discussing the incident and communicating the desired message; and (ii) a seminar for certain FTB employees on workers rights in cases of layoff and dismissal to be conducted by the WRC.

Current Status

An article discussing the February dismissals was first published in the company newspaper on August 5, 2009, but did not make clear the company's responsibilities under the labor law in the case of a layoff. After the WRC pointed out this inadequacy, Freetrend agreed to publish a second article that would make clear the company's commitment to follow the legally-required lay-off procedures in the future. An article to this effect was published by Freetrend in the company newsletter on September 7, 2009.

On September 23, 2009, the WRC's China Director and a local resource person in Shenzhen conducted a seminar for 100 workers at the FTB plant, in three classes of forty-three, twenty-seven, and thirty-three employees. In addition to workers, compliance staff from both New Balance and Freetrend attended the session. In addition to educating workers on the Labor Contract law's provisions regarding layoff and dismissal, the WRC trainers held a question and answer session, during which employees mentioned certain other labor issues at the FTB facility. The WRC, in turn, shared the workers' concerns with Freetrend and New Balance compliance staff. Both Freetrend and New Balance indicated that they would follow-up on these issues through further dialogue with employees. The WRC has informed Crocs of these issues to ensure that that they are addressed, if present, in the company's facilities that produce collegiate licensed apparel.

¹² See, WRC, *supra*, n. 7.