

# Mattel, Inc.: Global Manufacturing Principles (GMP) – A Life-Cycle Analysis of a Company-Based Code of Conduct in the Toy Industry

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**ABSTRACT.** Over the last 20+ years, multinational corporations (MNCs) have been confronted with accusations of abuse of market power and unfair and unethical business conduct especially as it relates to their overseas operations and supply chain management. These accusations include, among others, worker exploitation in terms of unfairly low wages, excessive work hours, and unsafe work environment; pollution and contamination of air, ground water and land resources; and, undermining the ability of natural government to protect the well-being of their citizens. MNCs have responded to these accusations by creating voluntary codes of conduct which commit them to specific standards for addressing these issues. These codes are created at both the industry-wide and the individual company level. Unfortunately, these codes have generated little credibility and public trust because their compliance claims cannot be independently verified, and they lack transparency and full public disclosure. In this article, we present a case study of the voluntary code of conduct by Mattel, Inc., the world's largest toy company. The code, called the Global Manufacturing Principles (GMP), confronts the general criticism leveled against voluntary codes of conduct by (a) creating detailed standards of compliance, (b) independent external monitoring of the company's compliance with its code of conduct, and (c) making full, and uncensored public disclosure of the audit findings and company's response in terms of remedial action. We present a detailed account of how Mattel's voluntary code of conduct was created, implemented, and ultimately abandoned over 9 years. We provide an evaluative analysis of the company's GMP compliance throughout its life span, which suggests a bell-shaped curve, where early top management commitments were met with pockets of resistance from operational groups, who were concerned about balancing GMP compliance efforts with traditional performance criteria. The early stage response from Mattel's top management

was quick and supported with the requisite resources. As a result, the compliance process accelerated, becoming increasingly more robust and effective. The success of code compliance and increased transparency in public disclosure energized field managers with a sense of professional satisfaction and publicly recognized accomplishments. The decline in GMP compliance was equally steep. When all the easily attainable targets had been reached at the company-operated plants, addressing vendor plants' compliance presented a new set of challenges, which taxed corporate resources and management commitment. It would seem that value-based and ethics-oriented considerations, i.e., doing the right thing for the right reason, were no longer the driving force for Mattel's management. Mattel did not see any economic benefit from its proactive stance, when competitors did not seem to suffer adverse consequences for not following suit. The final contributing factor to the code's abandonment was a widely publicized series of product recalls which absorbed top management's attention.

**KEY WORDS:** voluntary codes of conduct, sweatshops, outsourcing, supply chain management, corporate accountability, third party audits, Mattel, Inc., toy Industry, manufacturing in China, Malaysia, Thailand, and Indonesia, corporate culture, top management and management incentives

## Introduction

In November 1997, Mattel announced the creation of a global code of conduct for its production facilities and contract manufacturers. Called the Global Manufacturing Principles (GMP), the code covered such issues as wages and hours, child labor,

forced labor, discrimination, freedom of association, legal and ethical business practices, product safety and product quality, protection of the environment, and respect for local cultures, values, and traditions.

At the time of the GMP announcement, Mattel was the world's largest producer of toys in the world. With \$4.5 billion in annual revenue, the company was the worldwide leader in design, manufacture, and marketing of children's toys. Headquartered in El Segundo, California, Mattel has offices in 36 countries and markets its products in more than 150 nations around the world.

This case study offers a detailed account of how a company's voluntary code of conduct was created, implemented, and ultimately abandoned over a period of approximately 9 years.<sup>1</sup> It started out as a highly innovative response to societal concerns and challenged the toy industry's routine pledges of code compliance, which were rarely, if ever, independently verified and publicly reported. Moreover, this situation was not confined to the toy industry, but was endemic to other industries where large multinational corporations (MNCs) were establishing long supply chains and outsourcing operations in the emerging economies to take advantage of cheap labor and lax enforcement of health and safety conditions, pollution and other environmental protection standards.

In one sense, Mattel's code was not significantly different than a host of other codes of conduct that were sponsored by individual companies and industry groups from advanced countries with large manufacturing and procurement operations in low-wage countries with abundant supply of young workers. In large part, these codes appeared to have been created to assuage public opinion that these businesses were not exploiting workers by forcing them to work under sweatshop-like conditions. There was, however, little effort to implement these codes or show demonstrable improvement in the alleged abuses. Mattel, however, took a major step to move beyond the "me too" type of code of conduct. Mattel's GMP was quite different in one important aspect, i.e., Mattel committed itself, its strategic partners and primary suppliers, to comply with all the provisions of the GMP.

The second aspect of this case study is an evaluative analysis of both the achievements and shortfalls

in the company's code compliance during its short life of 9 years. The life cycle of the code, from its inception to abandonment, suggests a bell-shaped curve. While early efforts were taken with considerable commitment on the part of top management, but with significant pockets of resistance from operational groups who were concerned about their own performance on GMP compliance, and how it would be balanced with their performance on conventional business criteria of cost efficiencies and profitability.

A detailed analysis of the monitoring activities over the entire period of code compliance under study would indicate that field managers responded to GMP compliance standards in terms of direct and indirect signals they received from the top management. In the initial phase of compliance, activities were slow and deliberate since most actions were new and *ad hoc*. However, once the policies and procedures were established, they resulted in a steep learning curve. The initial phase also had strong oversight interest from top management including a representative of Mattel's board of directors, and called for frequent reporting. The response from top management was also quick and was supported with additional physical and human resources. The process accelerated and became more robust and effective. The success of code compliance and increased transparency in public disclosure energized field managers with a sense of professional satisfaction as they noted market recognition of their efforts, increase in public trust, and enhanced corporate reputation.

Unfortunately, the decline in the company's commitment to code compliance and transparency was equally steep. By the middle of the code's life cycle, it became apparent that all the easily attainable goals had been attained and further progress would be incremental and accommodated in normal business operations. Moreover, some of the initial stage expenditures that were designed to bring the company-owned and controlled plants to GMP standards had resulted in significant overall improvement in code compliance. The next phase, starting at the peak of the code life cycle of the bell-shaped curve presented a new set of challenges. It would require additional resources and top management commitment to bring vendor plants to improve their compliance efforts.

From our perspective, two other factors had a strong bearing on Mattel's decision to discard public disclosure of its code compliance activities.

1. The company's top management did not see any economic benefit from its proactive response to code compliance when other companies in the industry did not seem to suffer adverse consequences for not pursuing a robust and transparent form of code compliance. Thus, the company had to justify its GMP-related actions as "the right thing to do," a position that required a sustained level of value-based ethical commitment.
2. Mattel's top management was distracted with other issues pertaining to its manufacturing and marketing activities, which had strong and potentially negative impact on corporate reputation. Mattel was engulfed in a product recall of 17.4 million toys because of loose magnets that could be swallowed by children. The company also recalled another 2.2 million toys because of impermissible levels of lead in the toys. It was the biggest recall in the company's history. As if all this adverse publicity was not enough, one of Mattel's senior executives made a widely publicized public apology to Chinese authorities for inadvertently blaming China's weak regulation of that country's toy factories (Press Trust of India, 2007; Story, 2007; Story and Barboza, 2007).

#### *Antecedents to the creation of Global Manufacturing Principles*

Public concerns about worker exploitation and environmental degradation arose with the expansion of outsourcing and production in emerging economies where poverty, abundant labor, and need for job creation provided unprecedented opportunities for large MNCs to shift production from high-wage countries to low-wage countries.

Starting with isolated complaints from civil society organizations, human rights groups, and organized labor in the mid-eighties, the anti-sweatshop movement became a major force by early nineties in the United States, Canada, Europe, and other industrially advanced countries. Global companies were under fire for operating factories with working

conditions that violated basic human rights and labor laws in terms of wages and working conditions. Instances of worker exploitation and employment of underage workers were widespread.

For example, in the South Pacific Island of Saipan, the first assault was on companies that were characterized as labor intensive and required relatively simple and mature technologies requiring relatively smaller capital outlays. However, the protest movement soon engulfed high technology industries, where environmental contamination was a primary concern. Levi Strauss and Co. was accused of practicing "slave labor" (Schoenberger, 2000). In Indonesia, Nike was being derided for its poor treatment of workers. Asian American Free Labor Institute-Indonesia (AAFLI) was appointed by the U.S. Agency for International Development (USAID) to conduct a study related to worker treatment in East and Southeast Asia. The study found that Nike paid the lowest wages to its factory workers. This led to international campaigns against sweatshop conditions in Nike factories (NBOER, 2004). Levi established a code of conduct in 1991 after being reproached by media scandals (Levi Strauss & Co.). This was followed by Nike, which also established a voluntary code of conduct in 1992. Similar concerns were expressed against other companies and became objects of public reprobation. Another group discovered that Kathy Lee Gifford, a talk-show host and a celebrity, owned a clothing line made in sweatshops. Big names in the apparel industry like Wal-Mart, Kmart, Gap, and others were implicated in profiting from sweatshop-like manufacturing operations. Given the highly recognizable nature of these brands, International Labor and Human Rights Organizations launched a campaign against these and other companies. President Clinton formed the White House Apparel Industry Partnership in August 1996 to end sweatshops (United States Department of Labor, 1997). Organizations like National Labor Committee (NLC), Fair Labor Association (FLA), United Students Against Sweatshops (USAS), and Campaign for Labor Rights (CLR) were highly involved in castigating labor abuses (La Botz, 2007).

#### *Crisis at Mattel*

In line with apparel and footwear industries, the toy industry had also taken steps to respond to public concerns with regard to sweatshop-like conditions and

worker exploitation in toy manufacturing factories in China and other developing countries. These efforts were quite similar to those of other industries in that codes of conduct were created with tremendous fanfare but with insufficient effort to improve and monitor actual working conditions in those factories.

The crisis at Mattel occurred in December 17, 1996 (Barboza and Story, 1997; NYT, 1997). The company was caught off-guard by an investigative report aired by NBC's news program Dateline on December 17, 1996. An Indonesian factory that manufactured toys for Mattel was found to have employed underage workers who were also working long hours and doing excessive overtime. Although Mattel disputed some of the findings of the investigative report, it also realized that it must provide a more meaningful response in terms of corrective action.

Companies are more likely to respond forcefully, and even take radical action, when they are confronted with an external crisis, which has the potential of adversely impacting their core business operations and a diminution of the corporate reputation. In that sense, Mattel was no exception. The result was the creation of Mattel's GMP (See Exhibit 1).

#### Exhibit 1

##### **Global Manufacturing Principles, Mattel, Inc., 1997**

These manufacturing principles sets standards for every facility manufacturing our products in every location in which they are produced. Compromise is not an option. *Wages and hours:* All Mattel factories and vendors must set working hours, wages, and overtime pay that are in compliance with governing laws. Workers must be paid at least the minimum legal wage or a wage that meets local industry standards, whichever is greater.

While overtime is often necessary, in consumer product production, Mattel factories and vendors must operate in a manner that limits overtime to a level that ensures humane, safe, and productive working conditions. Overtime, if necessary must be paid in accordance with local laws.

*Child labor:* No one under the age of 16 or under the legal age limit (whichever is higher) may be allowed to work in a facility that produces products for Mattel. Simply stated, Mattel creates products for children around the world – not jobs.

We encourage the creation of apprenticeship programs tied to formal education for young people as long as students will in no way be exploited or placed in situations that endanger their health or safety.

#### Exhibit 1 continued

*Forced labor:* Under no circumstances will Mattel, Inc., use forced or prison labor of any kind nor will we work with any manufacturer or supplier who does.

*Discrimination:* Discrimination of any kind is not tolerated by Mattel, Inc. It is our belief that individuals should be employed on the basis of their ability to do a job – not on the basis of individual characteristics or beliefs.

We refuse to conduct business with any manufacturer or supplier who discriminates either in hiring or in employment practices.

*Freedom of association:* Mattel is committed to abiding by all the laws and regulations of every country in which we operate. We recognize all employees' rights to choose (or not) to affiliate with legally sanctioned organizations or associations without unlawful interference.

*Working conditions:* All Mattel, Inc., facilities and those of its business partners must provide a safe working environment for their employees. Facilities must engage in efforts including:

- Complying with or exceeding all applicable local laws regarding sanitization and risk protection and meeting or exceeding Mattel's own stringent standards.
  - Maintaining proper lighting or ventilation.
  - Keeping aisles and exits accessible at all times.
  - Properly maintaining and servicing all machinery.
  - Sensibly storing and responsibly disposing of hazardous materials.
  - Having an appropriate emergency medical and evacuation response plan for its employees.
  - Never using corporal punishment or any other form of physical or psychological coercion on any employee.
- Facilities that provide housing to their employees as a benefit of employment must ensure that housing be kept clean and safe.

*Legal and ethical business practices:* Mattel will favor business partners who are committed to ethical standards that are compatible with our own. At a minimum, all Mattel business partners must comply with the local and national laws of the countries in which they operate.

In addition, all of our business partners must respect the significance of all patents, trademarks, copyrights of our and others' products and support us in the protection of these valuable assets.

*Product safety and product quality:* All Mattel, Inc., business partners must share our commitment to product safety and quality and must adhere to those operational and workplace practices that are necessary to meet our stringent safety and quality standards.

## Exhibit 1 continued

*Environment:* Mattel, Inc., will only work with those manufacturers or suppliers who comply with all applicable laws and regulations and share our commitment to the environment.

*Customs:* Because of the global nature of our businesses and our history of leadership in this area, Mattel, Inc., insists that all of our business partners maintain a strict adherence to all local and international custom laws. Our business partners must comply with all import and export regulations.

*Evaluation and monitoring:* Mattel, Inc., is committed to ensuring that all facilities manufacturing our products meet or exceed our GMP and we will audit all facilities to ensure compliance. Consistently, we insist that all manufacturing facilities provide us with:

- Full access for on-site inspections by Mattel or parties designated by Mattel.
- Full access to those records that will enable us to determine compliance with our principles.
- An annual statement of compliance to our GMP signed by an officer of the manufacturer or the manufacturing facility.

Acceptance of and compliance to the Mattel GMP is part of every contract agreement signed with all of our manufacturing business partners.

*Compliance:* These principles are intended to create and encourage responsible manufacturing business practices around the world – not serve as a guideline for punishment.

We expect all of our manufacturing business partners to meet these principles on an ongoing basis. At the same time, our current business partners can expect us to work with them to effect change if certain aspects of the principles are not being met. Future business partners will not be engaged unless they meet all of our manufacturing principles.

If Mattel determines that any of its manufacturing facilities or any vendor has violated these principles, we may either terminate our business relationship or require the facility to implement a corrective action plan. If corrective action is advised but not taken, Mattel will immediately terminate current production and suspend placement of future orders.

In the case of Mattel, two distinguishing elements influenced its design of the new code of conduct. The company's products were aimed at children and the company emphasized children and family values.

Therefore, it could not be seen to be undermining these values by employing children and underage workers to make toys under sweatshop conditions. The company also had a strong CEO who favored entrepreneurial approaches to business strategy and operations. Mattel's board included a number of directors who were imbued with the ethics of corporate social responsibility and were supportive of GMP. Finally, the company's employees generally took pride in being part of the company.

*Putting thoughts into action*

*Establishment of Mattel Independent Monitoring Council*  
Mattel's GMP called for the creation of an independently and externally based monitoring system that would verify Mattel's compliance with its code of conduct in a manner that would be credible to the public and engender trust in Mattel's GMP-related performance claims. The exploratory process within Mattel led the company to identify Prof. S. Prakash Sethi as someone who could help the company in creating a credible process of code implementation that would be trusted by the public. Sethi had long been identified as a strong advocate of voluntary codes of conduct, provided they could be implemented in an effective and transparent manner, and where companies could be held accountable for compliance (Sethi, 2003).

Mr. Sean Fitzgerald, Mattel's Vice President of External Communications initiated contact between Sethi and Mattel. In an interview with the New York Times, Sethi recalled "They asked me if I could work with them, and I said, 'What do you mean, work with you?' They said, 'We have a problem: we want to make sure that we are doing the right thing, and that the public believes we are doing the right thing (Dee, 2007).'"

After some serious soul searching, Sethi conveyed his willingness to work with Mattel. The company would commit itself to three initiatives in implementing the code.

1. The GMP-related compliance efforts by Mattel, its strategic partners, and primary suppliers would be audited by an independent outside group of respected and knowledgeable experts. This group would have complete access to all



the facilities, workers, and supervisors, and payroll and financial records pertaining to the plants owned and operated by Mattel, its strategic partners, and primary suppliers.

2. The external monitoring group would have complete discretion in making its findings public, both as to their content and frequency.
3. GMP audits would not be a one-time phenomenon. Instead, they would be undertaken on a regular basis as an integral part of the company's operational philosophy.

Sean Fitzgerald was sold on what he called "the concept of Prakash." According to Fitzgerald, "You've got to have a strong sense of self in order to be successful in an endeavor like that. And Prakash has got that going on." Mr. Fitzgerald briefed Mattel's executives at the corporate headquarters in El Segundo, California on his discussions with Prof. Sethi and received their concurrence to proceed with the project (Dee, 2007).

Prof. Sethi was invited to visit Mattel's headquarters and to meet with top management. The resultant discussions led to the establishment of the Mattel Independent Monitoring Council (MIMCO), the precursor to the International Center for Corporate Accountability (ICCA). The council comprised three members with Prof. S. Prakash Sethi as its chairperson, and the other two members were Prof. L. Murray Weidenbaum and Rev. Dr. Paul F. McCleary.

In a press release following the creation of MIMCO, Mattel also commented on the positive aspects of the monitoring process. Jill Barad, Mattel's CEO stated, "Mattel is committed to improving the skill level of the workers in our facilities so that they, in turn, will experience increased opportunities and productivity." According to Joseph Gandolfo, then President of Mattel's Worldwide Manufacturing Operations, "These principles are intended to create and encourage responsible manufacturing business practices around the world – not serve as a guideline for punishment. However, manufacturers that do not meet our standards, or refuse to take swift, corrective action to do so, will no longer work for Mattel (PR Newswire, 1997)."

As part of its overall strategy of code compliance, Mattel's top management also undertook to:

- (a) make compliance with the GMP an integral part of management evaluation and compensation;
- (b) develop training procedures and information systems by which all levels of the company's managers and employees would be familiarized with these instructions and implementation procedures;
- (c) constantly revise and improve these instructions and operational procedures in light of experience gained from its own operations and those of other companies facing similar operational challenges in countries where Mattel has its operations, and,
- (d) verify that all of the company's operations, and those of its major suppliers and strategic partners, remain in full compliance at all times with the GMP and the Company's implementation procedures and instructions.

#### *Putting principles into practice*

Transforming a two-page document, which consisted of broad ethical declarations into detailed operational standards that would not only specify process, but even more importantly, require measurable outcomes, was quite complex and an enormous learning experience. According to Sethi, "It was totally unprecedented. Really intoxicating, I was inventing everything as I went along. There just were not any systems of its kind. Nobody could say, 'It can't be done' (Dee, 2007)."

The process required that the company engage its various operational divisions, which would be impacted with costs and benefits from complying with the code. Similarly, there were considerable differences of opinion among the senior managers in the corporate headquarters and those in the field as to the potential benefits and risks of breaking the prevailing industry mold, and whether in the end, the company would even gain anything by way of public trust in the implementation of this program.

Mattel set up two task forces, one in El Segundo and the other one in Hong Kong, to work with Sethi's group to create operational standards. The two task forces comprised more than 50 managers and technical experts. This group, along with

MIMCO, worked extensively over a 12-month period to create detailed operational standards and performance measures, and to secure agreement with Mattel's top management and field managers, as to those standards.

The newly devised standards had to meet four criteria:

1. *The standards must be quantifiable and objective in measuring and evaluating performance.* In other words, two different people observing compliance with a given criterion must draw similar conclusions.
2. *They must be outcome-oriented.* It is not enough to indicate that moneys are being spent or that policies and procedures exist. Rather, the plant management is required to show that there are so many bathrooms per 100 workers, so many square feet of living space per worker in a dormitory, and that the injury rate per 1000 worker-hours meets industry standards.
3. *At a minimum, these standards must meet the legal criteria mandated by the labor and environmental laws of the country where a plant is located.* Where country-specific standards do not exist, or are lower than Mattel standards, local plants must meet Mattel's own standards. As a long-term proposition, Mattel must endeavor to have its plants meet or exceed the best industry practices prevailing in their specific regions or localities.
4. *The standard-setting process is dynamic and interactive.* Standards of performance must continue to evolve in light of experience gained from existing operations, competitor conduct, and the company's desire to continue building on its leadership position. In addition, standards must evolve to meet changing societal expectations because of new data and conduct of major players in the industry, NGO community, public opinion, and behavior of host country governments.

The end product was the creation of an audit protocol, including a detailed 75-page checklist for quantifying conditions inside every one of Mattel's factories and vendor plants.

Are eyewash stations and safety showers installed in areas of corrosive material use (e.g., battery servicing

areas, cooling towers, storage of corrosive material, electroplating) and in high-volume solvent usage areas (e.g., paint mixing, chemical storage and dispensing, solvent distillation)?

By all accounts, both Mattel and Sethi's group fought energetically for their positions. But in the end, in return for the promise of restored public trust, Mattel was willing to let Sethi be Sethi. It would be wrong to say he is abrasive – on the contrary, he is chatty and hospitable in person – but he is most certainly unafraid to be abrasive when the situation calls for it. He has no interest in ingratiating himself with those in power. Jim Walter, senior vice president for global product integrity at Mattel, who has been in constant contact with Sethi and his staff for the past seven years, calls him “an appropriately positioned thorn in our side (Dee, 2007).”

This process led to the development of more than 200 specific standards. They define the compliance parameters for each principle and cover all aspects of manufacturing operations; environment health and safety standards; worker hiring and training; working conditions; working hours, performance bonuses, wages, and overtime; conditions in dormitories and recreational facilities; and non-job-related skill-enhancement programs. The China document alone is 60 pages long. Similar compliance documents were prepared for 20 other countries where Mattel had operations. These documents are continuously revised in light of changes in local labor and environmental laws.

#### *Changes in Mattel's top management*

No sooner had the field audit process gotten underway, Mattel was rocked by a major financial crisis that led to a wholesale change in the company's top management. Early in 1999, Mattel's CEO, Ms. Jill Elikann Barad, made an ill-timed acquisition of the Learning Company, a maker of educational software for US \$3.8 billion (Miller, 2000). It was a controversial acquisition both for its price and potential fit with Mattel's existing business model. Soon the acquisition turned out to be a financial disaster, risking the future of the company as a going concern. Mattel was losing about a million dollars in cash daily. Mattel's CEO was forced to resign and in an effort to turn the company around, Mattel's board

of directors brought in a new CEO, Mr. Robert A. Eckert, then the president of Kraft Foods.

The new CEO faced major challenges in restoring the company's financial health and could easily have relegated the GMP to lower priority. Eckert, however, chose a different course. In his first meeting with MIMCO and his senior managers, Eckert declared, "I am a libertarian by conviction. I also believe that the corporation's freedom to manage its operations cannot be sustained without our assuming our social responsibility to the community (Sethi, 2003)." He indicated that Mattel would behave in all its actions with "unwavering integrity"<sup>2</sup> and that the company's commitment to the GMP remained unequivocal and undiminished. In an interview with New York Times, Eckert admitted that it would have been tempting to eliminate the program as a cost cutting measure when none of Mattel's competitors even bothered with it. "We had a pretty frank discussion about it," Eckert admits, but in the end he chose to keep it going. "We want to be contributing to the development of these societies," he told me, "not merely taking advantage of the fact that they're not as developed as we are" (Dee, 2007).

#### *Modification of GMP – explicit and implicit exclusions*

The new top management team re-focused the company's attention to its core business operations including better oversight and control of its global supply chain. Among the changes, the company issued four policy initiatives to enhance internal GMP compliance. These included a revised GMP (Exhibit 2); documents outlining the roles and responsibilities of Mattel Corporate Responsibility Organization Worldwide; Disney sourcing policies and procedures, which apply to all Mattel facilities and contractors that source Disney products worldwide; and, policies and procedures that apply to all Mattel facilities and operations that license Mattel-branded products.

#### Exhibit 2

##### **Global Manufacturing Principles. Mattel. Inc. 2001**

*Scope:* Mattel's GMP policy applies to all parties that manufacture, assemble, or distribute any product, or package bearing the Mattel logo.

#### Exhibit 2 continued

*Purpose:* GMP is the cornerstone of Mattel's ongoing commitment to responsible worldwide manufacturing practices. The establishment and implementation of GMP provides a framework within which all of Mattel's manufacturing must be conducted.

GMP provides guidance and minimum standards for all manufacturing plants, assembly operations, and distribution centers that manufacture, assemble or distribute Mattel products. GMP requires safe and fair treatment of employees and that all locations protect the environment while respecting the cultural, ethnic, and philosophical differences of the countries where Mattel operates.

*Introduction:* As "The World's Premier Toy Brands-Today and Tomorrow," Mattel takes pride in the quality of its products, its customer relationships, its employees, its communities and its global reputation, as well as the value built for its shareholders.

Mattel is committed to executing GMP in all areas of its business and will only engage business partners who share its commitment to GMP. Mattel expects all its business partners to enforce GMP, and will assist them in meeting GMP requirements. However, Mattel is prepared to end partnerships with those who do not comply. Compromise is not an option.

##### *Our values*

The foundation for the successful implementation of GMP lies within the Mattel core values. It is essential that the company's business partners share these values.

##### *We value:*

##### 1. Our consumers

The well-being of children is an inherent part of the reason that Mattel exists and this is reflected in all aspects of our business. A child's well-being is our primary concern in considering the quality and type of toys produced, and in the way Mattel toys are manufactured. At Mattel, we want to inspire children's imaginations and enrich their lives with our products. Accordingly, Mattel is committed to creating safe and quality products for children around the world. Mattel products will be manufactured in a manner which will meet its GMP stringent standards.

##### 2. Our work

We strive for excellence and creativity in every aspect of our business. Mattel understands that the implementation of GMP is an on-going process, and is committed to making continuous improvements to its GMP performance as the company strives for full compliance.

We are dedicated to a creative approach in addressing areas of particular concern and resolving compliance issues. We will protect the environment and continue to reduce our use of resources and materials. In every aspect of our business, we will conduct ourselves with unwavering integrity.



## Exhibit 2 continued

## 3. Our partners

We will share success with our customers, our suppliers, our shareholders, and the communities where we operate.

Our shareholders and customers demand that Mattel products are manufactured and assembled under ethical working and living conditions. Enforcement of the company's GMP policy illustrates to customers and shareholders that Mattel shares their concern and is committed to ensuring that Mattel products are manufactured under conditions that meet GMP standards.

We are also committed to supporting and working closely with our individual vendors in complying with GMP.

## 4. Ourselves

We operate with unwavering integrity and take ownership of all issues that pass in front of us. We are accountable for the results of our business and the development of our fellow employees. We are dedicated and committed to implementing GMP with honesty and have incorporated measures to ensure continual improvement in our performance. While the development of GMP is essential to success, enforcement of the code is equally as important. Mattel has initiated an extensive three-stage auditing process – that is overseen by an independent monitoring council – to thoroughly inspect both the company's-owned and -operated facilities around the world, as well as those of our contractors.

We will continue to refine GMP to ensure that all employees are treated fairly, with respect, and work under safe and healthy conditions that encourage dignity and pride for themselves and their workplace.

*Our commitments*

Mattel will operate its facilities in compliance with applicable laws and regulations of every country where the company operates. In countries where the laws are not well defined, Mattel has developed country-specific standards that govern our operations and those of the companies that manufacture, assemble, or distribute our products.

Mattel has defined the following basic standards of conduct to guide Mattel and each of its business partners' operations in implementing GMP. These standards are dynamic and evolving to ensure ongoing protection of employees and the environment.

## Exhibit 2 continued

1. *Hiring, wages, and working hours*

- a. *Work hours:* Mattel will comply with country laws. Overtime work must be voluntary.
- b. *Work week:* We will comply with country laws but require at least one rest day per week.
- c. *Wages:* Wages must meet or exceed legally mandated minimum wage. Wage rates for overtime work must also meet legally mandated rates.
- d. *Benefits:* All benefits provided to employees must comply with country laws.
- e. *Payment of wages:* Employees must be paid at least monthly. Accurate records for each employee's regular and overtime hours must be maintained either through time cards punched by each employee or through other similar systems. Pay records must include employee work hours; and every employee must be provided a pay stub with pay calculations and deductions clearly listed.
- f. *Deductions:* Deductions must comply with local laws. Deductions for company provided food and living must be reasonable, affordable and if employees choose to live and eat outside of the company facilities they will not be charged.
- g. *Hiring:* Every employee must be provided a written document which outlines their work hours, wages, wage calculations, benefits, costs for food and living, and length of employment contract. Mattel and its partners will not charge employment fees and we will monitor our hiring agencies to ensure that fees are reasonable.

2. *Age requirements*

- a. No one under the age of 16 will be employed. If the local law requires a higher minimum age, we will comply with the local law.
- b. In cases where employees are hired between 16 and 18 special considerations must include annual physicals and will exclude hazardous duties.
- c. A system must be in place to detect forged and false identity documents.

3. *Forced labor*

- a. Under no circumstances will forced or prison labor be used to manufacture, assemble, or distribute Mattel products. Each employee must be provided with a document stating that employment and overtime is voluntary.
- b. Mattel will not allow or condone physical or verbal abuse, or any form of physical or psychological coercion of employees.
- c. There must be a written grievance procedure in place.
- d. Every employee must be provided with general orientation on GMP as well as the local company code that includes: wages, working hours, dormitory rules, canteen procedures, grievance procedures, disciplinary procedures, safety training, evacuation, fire prevention, self-improvement opportunities, and a plant tour.

## Exhibit 2 continued

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**4. Discrimination**

- a. The location must have a procedure on hiring, promotion, and disciplinary practices that addresses discrimination. Discrimination or harassment on the basis of age, religion, sex, or ethnicity will not be tolerated.
- b. Mattel will make every attempt to further employee job skills through training.

The company will give strong preference to promotion from within the ranks of the current employees. No employee will be denied promotion opportunities for reasons of age, sex, ethnicity, or religion.

**5. Freedom of expression and association**

- a. Each employee has the right to associate, or not to associate, with any legally sanctioned organization.
- b. Management must create formal channels to encourage communications among all levels of supervisors and employees – without fear of reprisal – on issues that impact their working and living conditions.
- c. Senior managers must hold quarterly meetings with all levels of employees to share information and discuss plant-wide issues.

**6. Living conditions**

- a. Dormitories (if provided)
    - i. Every employee must be provided with adequate living space.
    - ii. Ventilation must be provided.
    - iii. Showers and bathrooms must be convenient, centrally located or in the room.
    - iv. Lockable storage space for each employee must be provided.
    - v. Hot water must be provided.
    - vi. Dormitories must be maintained, clean and safe.
    - vii. Safety hazards must be eliminated.
  - b. Canteens (if provided)
    - i. Canteen staff must have annual physical examinations.
    - ii. Canteen staff must wear clean clothing with proper protective equipment when serving food.
    - iii. Canteens must be clean, well lit, and free of food scraps.
    - iv. Refrigeration must be available if perishable food is stored.
    - v. Tables and chairs must be provided.
    - vi. Meals provided must meet nutritional requirements.
- 

## Exhibit 2 continued

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**7. Workplace safety**

- a. There must be trained or certified safety professionals and a written safety program must be developed.
- b. Combustible materials must be properly handled with special precautions taken in spraying and mixing areas.
- c. Machines with revolving or moving parts must be guarded and employees will receive special training on the use of this machinery.
- d. Hazards must be eliminated where possible. Employees must be provided and trained on the use of personal protective equipment where hazards cannot be fully eliminated.
- e. Mattel will identify all hazardous materials and properly train employees on the appropriate procedures for handling these materials.
- f. Safety training must be conducted for special work categories (industrial trucks, electricians, maintenance, painters, molding operators, etc.).
- g. Employee exposure to chemicals and vapors must be below legal requirements or Mattel Standards whichever is the most stringent. In special cases where ventilation cannot eliminate the exposure, respiratory protection will be used and employees trained.
- h. All accidents must be investigated and corrective actions documented.
- i. All locations must continuously reduce accident rates and have specific targets on reductions.

**8. Health**

- a. In locations where there are more than 1000 employees, there must be an on-site medical facility for routine medical treatment and work-related injuries. In locations where there are less than 1000 employees treatment must be available to employees within 15 min if there is not a clinic on-site.
  - b. The facility must have lighting which meets Mattel's standards or local requirements, whichever are higher.
  - c. Temperatures must be measured during hot and cold seasons and if they exceed local or Mattel standards corrective actions must be taken.
  - d. Noise must not exceed 85 dB. Hearing protection must be used in any areas that exceed this limit. If the local limit is lower, the lower limit will be used.
-

## Exhibit 2 continued

9. *Emergency planning*

- a. Emergency plans for evacuation, spills, and natural disasters must be current and identify key responsibilities.
- b. Emergency evacuation signals must be understood and audible in all locations of the facilities.
- c. Emergency exits must meet local or Mattel standards.
- d. Emergency lighting must provide immediate (within 5 s) and sufficient lighting to allow evacuation.
- e. Fire extinguishers must be provided and employees designated to use fire extinguishers must be trained.
- f. Employees must be trained on reporting emergencies and evacuation procedures.
- g. Emergency equipment and respective documentation must be maintained.
- h. Special protective and prevention systems like “hot work” must be used when open flames are present.

10. *Environmental protection*

- a. Trained environmental personnel must be assigned to manage the areas of air and water emissions and waste management.
- b. Hazardous wastes must be properly contained, stored and only disposed of at approved facilities.
- c. Water discharges must meet local requirements or Mattel’s standards.
- d. Mattel will quantify its wastes and continually reduce them.
- e. Air emissions must meet local requirements or Mattel’s standards.
- f. Any and all spills or releases must be immediately cleaned.
- g. Odors and noise that cause undue disruption to the community must be eliminated.
- h. Plans to handle environmental emergencies must be current and identify key responsibilities.

11. *Evaluation, corrective action, and monitoring:*

- a. Mattel and its business partners will undergo an audit process to assess compliance with GMP. This process must include a corrective action plan to ensure that audit findings are corrected and GMP compliance achieved. Mattel will work closely with all business partners to ensure that corrective actions are completed in a timely manner.
- b. In cases where corrective actions are not taken in a timely manner, Mattel will identify alternative suppliers. However, Mattel is prepared to terminate any operation or partnership where compliance is not achieved within the time frame agreed upon. Mattel will not engage potential business partners unless they meet the company’s stringent requirements or are committed to achieving full compliance.

## Exhibit 2 continued

c. Mattel’s commitment to the public includes verification audits by an independent monitoring organization to assess the GMP performance of Mattel and its business partners. An independent monitor will conduct periodic evaluations of a select number of locations of its choosing to verify compliance with GMP standards. They will be provided with complete access to all information and facilities in order to make an evaluation of Mattel’s performance in ensuring that Mattel locations and those of its partners meet GMP standards. The independent monitor has the discretion to periodically issue reports to the public on our progress<sup>a</sup>

<sup>a</sup>Committee on Energy and Commerce (2007, August 22). Letter to Mr. Robert A. Eckert re: Subcommittee on Commerce, Trade, and Consumer Protection of the Committee on Energy and Commerce Hearing. Retrieved December 2007, from <http://energycommerce.house.gov/images/stories/Documents/PDF/selectedlegislation/Mattel.082207.pdf>; Normile, Bob. (2007, September 5). Response of Mattel, Inc., to the August 22, 2007 Information Request from the Subcommittee on Commerce, Trade, and Consumer Protection. Retrieved from <http://energycommerce.house.gov/images/stories/Documents/PDF/selectedlegislation/Mattel.090607.response.082207.pdf>; Chairman Dingell at the Subcommittee on Commerce, Trade, and Consumer Protection hearing entitled “Protecting Children from Lead-Tainted Imports” (2007, September 19). Retrieved from [http://energycommerce.house.gov/index.php?option=com\\_content&view=article&id=114&catid=18:platforms&Itemid=58](http://energycommerce.house.gov/index.php?option=com_content&view=article&id=114&catid=18:platforms&Itemid=58); Hearing before the Subcommittee on Commerce, Trade, and Consumer Protection (2007, September 19) (testimony of Robert A. Eckert). Retrieved from <http://energycommerce.house.gov/images/stories/Documents/Hearings/PDF/110-ctcp-hrg.091907.Eckert-testimony.pdf>; Consumers Union. (2007). Retrieved from <http://energycommerce.house.gov/images/stories/Documents/PDF/selectedlegislation/FoodSafety.ConsumersUnionReport.pdf>; Edelman, Adam and Nichols, Adam. (2007, August 15). Big Recall Rerun by Mattel: 9.3 million more toys from China have lead paint or deadly magnets. Daily News. Retrieved from <http://www.nydailynews.com/news/national/2007/08/15/2007-08-15bigrecallrerun.html>; Barboza, David. (2007, September 11). Problems Go Beyond Lead Paint, Canadian Study Says. New York Times. Retrieved from <http://query.nytimes.com/gst/fullpage.html?res=9404E5DC1F31F932A2575AC0A9619C8B63>.

### *Explicit exclusions*

The original GMP (Exhibit 1) included product safety as an integral part of the GMP provisions. In practice, however, both Mattel and MIMCO agreed that initial focus would be on worker employment, health, and safety issues as well as monitoring of emissions from factories. MIMCO felt that this was a good arrangement since it was in Mattel's own interest to ensure that its toys were safe and met all regulatory requirements applicable in U.S. and other toy importing countries.

As things turned out, MIMCO's assumptions were not borne out by realities. The culture of product safety is not so thoroughly embedded in developing countries where expectations toward adherence to product safety standards are generally lower than those prevailing in industrially advanced countries. Given the fact that factories in China need constant monitoring to ensure compliance with local employment laws, neither the company nor MIMCO should have assumed that factory owners would not be tempted to cut corners and save money using substandard materials and lower safety standards in the manufacturing process.

As the world's largest toy manufacturer, Mattel has had more than its share of safety-related product defects. Mattel also has had a long history of contentious relations with regulators, notably the Consumer Product Safety Commission (CPSC), which has repeatedly charged the company with violating its rules for timely notification pertaining to safety-related product defects. This contention is consistently denied by the company, which sticks to its own interpretation of the regulatory requirements for timely disclosure (CNN Money, 2007). Nevertheless, the company had paid numerous fines for alleged violations, and in a number of cases settled with individual consumers (Casey, 2007). The latest in this sequence of events was a civil penalty of \$2.3 million paid by Mattel in 2009 for violating Federal Lead-paint ban. "In retrospect," Murray Weidenbaum, a former MIMCO board member, told Jonathan Dee of the New York Times, "the mission we were assigned was narrower than perhaps it should have been. We focused on the working conditions, because that was our task, and because critics at the time were focusing on it – child labor, prison labor, all that. It turns out we missed the big

picture, which is the nature of the product" (Dee, 2007).

### *Implicit exclusions*

The preamble to Mattel's revised GMP states:

*Scope:* Mattel's GMP applies to all parties that manufacture, assemble or distribute any products or package bearing the Mattel logo. Similarly, Section II of revised GMP states: "Mattel and its business partners will undergo an audit process to assess compliance with GMP....Mattel's commitment to the public includes verification audits by an independent monitoring organization to assess the GMP performance of Mattel and its business partners [emphasis added] (See Exhibit 2)."

In practice, however, this did not turn out to be the case. From the very start of the independent monitoring process, Mattel resisted every effort by MIMCO to provide information about its licensing partners, i.e., companies that make products using Mattel logo, e.g., Barbie sleepwear, children's furniture. The company initially argued that given the enormity of the task at hand, MIMCO should focus on auditing Mattel-owned and controlled plants and vendors that make products for Mattel. It was also suggested that Mattel was setting up its own internal organization to monitor all of its licensees and thus any audits by MIMCO should be postponed until such time that Mattel had completed its in-house organization and implemented initial audits.

However, despite repeated requests, Mattel never provided MIMCO (and its successor ICCA) with any information about the scope of its licensee operations; the extent to which they have been audited by Mattel's in-house auditing organization; and, the overall state of licensed compliance with GMP. During the period, 1999–2008 when MIMCO (and ICCA) were responsible for GMP external audits, there were numerous incidents and news media reports of worker abuse and poor factory conditions in Mattel's licensee factories. All of these were handled by Mattel without any involvement by MIMCO or ICCA. It should also be noted that Mattel does not separately disclose revenues from licensee operations in its financial statements. They are consolidated in the company's total sales. However, the consensus is that these operations account for almost 50% of Mattel's total sales.

*Framework for a viable external audit regimen*

A basic premise of MIMCO's audit regimen was that Mattel would create an in-house auditing organization that would be responsible for conducting GMP compliance audits of its own plants and those of its vendors and licensees. MIMCO would in fact be verifying the quality and veracity of audits conducted by Mattel's own people. This is a critical distinction because any shortfalls in factory compliance discovered by MIMCO would also imply a failure on Mattel's part in carrying out its own auditing and monitoring responsibilities.

MIMCO established a systematic 3-year cycle to meet its obligations for external audits. The first year of the cycle would concentrate on Mattel facilities. These would include all of the company-owned plants and other plants in which Mattel controlled 100% of the output. The second year would focus on a sample of the plants owned and operated by Mattel's strategic partners and primary suppliers and from which Mattel buys 70% or more of the plant's output. The third year of the audit cycle would focus on a statistically selected sample of second-tier plants from which Mattel buys between 40 and 70% of the plant's output. This audit cycle would be repeated on a 3-year basis. This approach ensures that every plant in a group has an equal chance of being selected for a verification audit where no plant has prior knowledge of being selected. Vendor Plants with less than 40% of the output dedicated to Mattel products were excluded from MIMCO audits. Plants in each group would be subjected to MIMCO audits once every 3 years. In addition, MIMCO had complete discretion to include additional plants in its audit sample in order to arrive at a more accurate picture of how well Mattel's strategic partners and primary suppliers were complying with GMP requirements.

*MIMCO's audit protocols*

MIMCO had to create its own audit protocols and audit instruments. The objective was to ensure that MIMCO audit reports were comprehensive and provided the public at large a fair, objective, and unbiased picture of conditions in the audited plants. These comprised four elements: Management Compliance Reports; Payroll and Personnel Files

Desk Audits; Systematic Walk-Through Examination of the Plant and Dormitories; and one-on-one Worker Interviews (Exhibit 3).

## Exhibit 3

**MIMCO(ICCA) Audit Protocols**

The implementation of Mattel's GMP is carried out according to detailed standards of performance as prescribed by detailed checklists tailored to meet the specific legal requirements of each country as well and/or Mattel's GMP, whichever is more stringent.

*Pre-audit preparation*

Prior to the on-site audit, ICCA formally requests information from the plant management regarding its operational and human resource management practices. The Management Compliance Report (MCR), is a standard document which contains detailed information on all aspects of the plant's operations, the extent of management's compliance with various GMP provisions, details of any shortfalls, and management's plans for corrective action. ICCA also reviews reports of all in-house audits conducted by Mattel's internal audit department.

*The field audit*

Intent of the field audit is to ensure that all workers receive wages for regular and overtime work as mandated by law; the factory operates within legal and GMP standards as to regular and overtime hours; and provides benefits as mandated by law and GMP standards. The field audit comprised four parallel activities. The first one is an audit of a randomly selected sample of workers personnel files and payroll records. Contracted professional auditors who have extensive knowledge of China's labor laws and local accounting practices conduct this audit under ICCA supervision. Where complex issues of interpretation of China's labor laws and regulations are required, ICCA relies on advice from its legal counsel in China.

The second element of the audit involves interviews with the same group of workers who were selected for the payroll and personnel file audit. Each worker is interviewed individually in a private, secured space to ensure complete confidentiality. A typical interview lasts around 45 min. The interview questionnaire was developed by ICCA and is designed to elicit information on all aspects of the workers' working and living conditions at the plant. This process allows for a comparison of the information contained in the plant's payroll records and personnel files, and the information elicited from the workers through the interviews. Professional interviewers, retained independently by ICCA and generally meeting the age and gender profile of the workers, conduct these interviews in the workers native language.



## Exhibit 3 continued

The third element of the audit is a thorough examination of the plant's policies, procedures, and practices with regard to environment, health and safety issues. The EHS audit entails:

- An evaluation of the MCR completed by plant management, indicating the extent of compliance with Mattel's applicable checklist;
- A "walk-through" of the plant; and
- Examination and verification of site history, permits, monitoring, surveillances, and compliance documentation as required by law.

China-based independent environmental engineers who are trained in China's laws and regulations in manufacturing operations conduct this phase of the audit under SICCA engineers' supervision. Inspection includes an examination of the general maintenance of the manufacturing facilities, storage, treatment and disposal of hazardous waste materials, hygiene in bathrooms, kitchen and eating facilities with particular emphasis on safety and health. The walk-through also includes a thorough inspection of the dormitories and recreational facilities in terms of hygiene, adequacy of space, worker comfort, privacy and security, and other related matters as deemed appropriate in specific situations.

The final element of the SICCA audit is a series of meetings with various functional managers which serve to confirm and clarify issues in the MCR and elaborate on the plant management's practices regarding issues that emerge during the field audit.

#### *Post-audit activities*

All audit documents are hand-carried to the New York offices of ICCA for analysis and report preparation. Initial findings are reported to Mattel to ensure factual accuracy. In case of a material error, ICCA revises the draft report before making it public. In other cases, Mattel responds with corrective action commitments. ICCA assesses this response and indicates the extent of follow-up to be undertaken by ICCA to ensure full and timely compliance. The audit report indicates the findings of the audit as well as Mattel's responses and commitments. In the event of a disagreement between ICCA and Mattel as to the nature of findings or the adequacy and timeliness of corrective measures, both perspectives are made public without any editing by ICCA or Mattel.

#### *Summary of audit findings*

The first round of audits was initiated in the second half of 1998 and was in the nature of dry runs. Their intended purpose was to familiarize both plant

managers and factory owners with the expectations of GMP audits and how they would be conducted. At the same time, it would provide MIMCO members with an understanding and appreciation of the field conditions they would face while conducting GMP audits.

The formal audits started in earnest in the latter half of 1998 and continued through 2008 when they were unilaterally discontinued by Mattel.<sup>3</sup>

To facilitate better understanding and comprehension of the audit findings, we have grouped them in four categories:

1. Mexico – All plants owned and operated by Mattel.
2. China – All plants owned and/or operated by Mattel.
3. China – All plants owned and operated by suppliers.
4. All plants owned and operated by Mattel in Indonesia, Malaysia, and Thailand.

#### **Mexico**

The first round of formal audits took place on August 2–6, 1999 and initially involved two plants. Montoi S.A. de V.C. in Monterrey and Mabamex S.A. de V.C., Tijuana. Both plants were dedicated to the production of Barbie dolls and other Mattel-branded toys. The Tijuana plant was moved to its current location in April 1998, and was still undergoing the process of "settling in." During the initial MIMCO visit to Monterrey, the audit team was shown the location and partial construction of a very large new Mattel plant titled MX3. The new plant incorporated all the activities from the old Monterrey plant. The first formal audit of MX3 was conducted on November 7–8, 2000.

The Monterrey factory had a peak employment of approximately 2300 workers, and the Tijuana plant around 2150 workers. These numbers were considerably reduced during the off-peak season.

MIMCO's audit found the Monterrey plant to be a well-managed facility and commended its management for its commitment to GMP standards. Montoi while being an old plant with non-air-conditioned workspace was also well-maintained and in general provided a clean safe environment.

Montoi met all of the important GMP standards with regard to the workplace, environment, and maintains detailed records on various aspects of manufacturing operations and employee status. Analysis of the plant's payroll records and worker interviews also confirmed that the Montoi plant met all regulations of the Mexican government as well as GMP standards with regard to the payment of wages for regular and overtime work. MIMCO's one-on-one confidential interviews with a randomly selected group of workers confirmed a high level of satisfaction with all aspects of their work at the plant.

The formal audit of the Tijuana plant (Mabamex) also revealed a satisfactory picture. The Mabamex plant satisfied all regulations of the Mexican government as well as GMP standards with regard to the payment of wages for regular and overtime work.

Mabamex was a well-maintained, clean and completely air-conditioned facility. A small group of workers, however, expressed concerns about excessive noise and poor ventilation. MIMCO's own inspection attributed these deficiencies to the plant's recent relocation. These deficiencies were soon rectified and confirmed by MIMCO.

At the time of the audit, MX3 was a brand new facility in the start-up phase with approximately 1500 workers during peak period. It is a very modern and completely air-conditioned facility; the factory manufactures large toys using primarily injection and blow molded parts. The workforce is predominantly female, and relatively young with low level of education and little prior work experience. The plant had high levels of worker turnover, i.e., 235% a year, which may go even higher during certain months.

The field visit turned out to be an unpleasant surprise, especially given the fact that it was a brand new facility. The new plant was already showing signs of severe neglect in both routine and preventive maintenance. Furthermore, the flow of materials, processing, waste handling, storage and disposal, suggested a disregard of normal safe handling procedures. The molding area of the plant was unkempt with oil spills on the floor, draining into an open channel. There were large amounts of make-shift electrical wiring and bare electrical connections. In several places, live electrical cords were lying across employee pathways. These conditions created an unacceptable level of hazard for workers and in-

creased danger of fire in the plant. The same level of neglect was also observed in kitchen, canteen, and dormitory facilities. There appeared to be little emphasis on the use of personal protection equipment (PPE). Most employees working in high noise contaminated areas did not wear earplugs. MIMCO also noticed open containers of volatile flammable liquids stored in assembly areas.

The plant was in full compliance with regard to working hours and payment of regular and overtime hours. In other areas of worker treatment, the MIMCO team found the factory's practices questionable. All MX3 workers, whether in molding or assembly areas, are required to stand through their entire work shifts. This was an unprecedented situation. In all of MIMCO audits of Mattel-owned and operated facilities in Asia and Mexico, it did not find a single plant where workers were not provided with some type of stool or chair and were instead required to stand through their entire work shift.

#### *Management's response to MIMCO's draft audit report*

MIMCO provided a report to Mattel's management. This was in accordance with established practice wherein the plant management or general managers have an opportunity to respond to MIMCO's findings. In response, for the first time, MIMCO experienced considerable pressure from the operational level managers to modify its draft report, suggesting we had over-reacted to isolated instances and that management had already identified many of these issues and was taking corrective action. MIMCO was also provided with a list of "changes in language" and urged to insert them in the draft report.

The response from Mattel's top management was short and swift. It asked for a 90-day period to fix the problems and invited the MIMCO team for a full-fledged follow-up audit. In a written response to MIMCO, Mattel stated:

We recognize that this report does not reflect favorably on the performance of our MX3 facility. There are a number of reasons that led to these conditions but none justify MIMCO's findings in November 2000. We will not accept this performance and will not make excuses.

The follow-up audit in February 2001 revealed a radically transformed factory. It would seem that plant management had paid careful attention to MIMCO's audit findings and addressed them in a systematic manner. MIMCO's overall observation was that in all essential areas, MX3 complied with the GMP.

During the 6-year period 2001–2007, MIMCO/ICCA conducted two rounds of audits covering all Mattel plants in Mexico. In general, these plants were found to comply with GMP standards. Where minor shortfalls were found, they were considered normal in any factory and were easily corrected.

## Indonesia

Mattel's Indonesian operations have undergone a series of changes during the period 1999–2008. These transformations involved both changes in product mix and plant restructuring. Mattel-owned and operated plants in Indonesia were audited by MIMCO/ICCA in February 1999, May 2002, and April 2008.

Initially, these plants were called Mattel Indonesia Cikarang Plant (MJS) and Mattel Indonesia Cikarang Baru Plant (MID). By 2008, the two plants were operating as PTMI East and PTMI West. The East plant is PTMI's major facility. Most of the West plant's employees and equipment were relocated into the East plant. Approximately, one-third of the West plant was still operative. The on-going production operations in the West plant primarily consist of injection molding, spray painting, and pre-assembly. The primary production processes at the East plant were molding, spray painting, final assembly and packaging. At the time of the third audit in April 2008, PTMI employed 7000 people. However, the work force would increase to 10,000 employees during production peak season. The work force consists of 65% permanent employees and 35% temporary contract workers. Female workers constitute 91% of the direct labor workforce. The average age is 31 years and no one under the age of 18 is employed.

While in Indonesia, during the second round of audits in May 2002, Mattel informed ICCA that it had outsourced some sewing operations to a pri-

vately owned factory located about 1.5 hour flight time from Jakarta. ICCA team was invited to visit the factory on an informal basis with the understanding that a formal audit would be conducted during the next audit round of the Indonesian plants. The visit indicated that the factory appeared to be well-managed with over 500 workers dedicated to manufacturing Mattel products. The team, however, did not conduct any worker interviews. Nor did it examine payroll records to ascertain employee wages and working hours, and the extent to which they complied with Mattel's GMP. Mattel did not include this factory in the third and final round of audits of the Indonesian plants and no further information was made available.

### *General findings*

Throughout the three audits, ICCA found the two plants to be in general compliance with GMP standards for physical work environment, health, and safety standards. The plants were also in compliance with GMP's requirements and Indonesian laws, with regard to wages for regular and overtime work and with the total number of work hours per week. There were some deviations from GMP compliance as applied to workers. These have been noted in the sections below.

### *Principal areas of concern and disagreement*

ICCA's concerns with regard to compliance with GMP were twofold. In some cases, the shortfalls and deficiencies identified by the audit team were rectified. However, in certain other areas where GMP non-compliance was considered serious, satisfactory corrective action was not taken.

### *Environmental protection, worker health and safety issues*

In the 1999 audit, it was noted that there was the presence of chemical odors, noise levels; although PPE was available, its usage was not being enforced. The 2002 audit showed no improvement: the noise levels, especially in the roto-casting area to be 90 dB, which was above the acceptable 85 dB level, but all employees in the area wore protective earplugs. The

2008 audit confirmed that the EHS problems noted in the previous audits were satisfactorily addressed except for the noise levels, which exceeded the Indonesian and Mattel in several locations.

#### *Dormitories*

The management and operation of dormitories presented a major area of disagreement between Mattel and ICCA, which remained unresolved during the entire cycle of three audits over a 9-year period. The principal areas of non-compliance pertained to (a) the maximum number of workers per room, and, (b) a mandatory requirement that certain workers must stay in the dormitories as a condition of their employment. Mattel's GMP requires that the number of workers be limited to a maximum of 12 per room (16 for grandfathered facilities). This was intended to provide the workers with a minimum level of privacy and to minimize noise level since the shift changes inevitably cause disturbance to the workers who are sleeping. It was found during all three audits that both dormitories were built to accommodate 30 workers per room. Although, the dormitory space allocated per employee met the GMP guidelines, the number of workers per room was far in excess of the 16 permitted in any one room.

In response to the first audit, Mattel indicated that suitable changes would be made in the re-configuration of the larger rooms. The second round of audit revealed that this change had not been made. By the time of the third audit round in April 2008, and despite its earlier promise, Mattel had failed to undertake changes in the dormitory configuration. At the conclusion of the third and last round of audits, Mattel again assured ICCA that the necessary changes in the dormitories would be made.

The second issue, which ICCA considered an even more serious violation of GMP, had to do with requiring workers to stay in the dormitory as a condition of their employment. When this issue was raised with the plant management during the first post-audit meeting, the management offered the following in defense of their policy:

- (a) Most of the workers, who are both young and female, come from villages and are not used to independent urban living. Their parents expect plant managers to provide these

workers with secure and safe living conditions. This rationale, however, fails to offer a justification for universal mandatory residency requirements, where local workers, old enough to be responsible for their actions, and, are married.

- (b) Plant management also argued that since workers accept the mandatory dormitory living as a condition of their employment, there was no violation *per se* of GMP standards.

MIMCO/ICCA disagreed with these contentions and noted its disagreement in the formal audit report. In response, Mattel agreed to find a mutually acceptable solution prior to the scheduled second round of audits.

The second round of audits noted some changes in the company's policies. Married and permanent workers were no longer required to stay in the dormitories. The relaxation of mandatory residency standard for married and permanent workers had resulted in the departure of a large number of workers to private housing, leaving the plant with unfilled dormitory space and a heavy fixed cost burden of maintaining these dormitories while generating even lower rental income.

By the third round of audit, the situation had not changed. ICCA's interviews with workers revealed that many workers chose to pay the dormitory rent to meet the mandatory residency requirement and still opted to rent private housing in the surrounding neighborhoods. This situation was also recognized and confirmed by the plant management in post-audit meeting with MIMCO/ICCA.

ICCA's experience with regard to the dormitory situation strongly suggested that while the nature of non-compliance with GMP was unambiguous, Mattel's top management was reluctant to enforce GMP standards upon the local managers. In ICCA's view, the primary consideration was money. Given the changing demographics, workers were no longer willing to stay in the dormitories. Consequently, the cost of maintaining empty dormitories was a burden that the company wished to avoid. However, the issue has since become moot as Mattel had cancelled its program of independent external audits by ICCA, and thus avoided the embarrassment of publicly disclosing its corrective action or lack thereof.

*Employee relations*

The 2008 audit showed that 10% of the interviewed workers were pressured to work overtime even when they were unwilling to do so. Mattel has assured ICCA that corrective actions will be instituted and communicated to prevent the elimination of unwilling overtime. Involuntary overtime and verbal abuse by floor level supervisors was not fully addressed by the time the 2008 audit was completed.

*Check-out time*

Another major discrepancy in compliance with GMP standards that has persisted over the entire audit cycle of 9 years had to do with electronic checkout time. Both plants have an electronic system whereby workers swipe magnetic cards to log their time for coming into the factory. However, their checkout time was not recorded by the computer system. This situation was identified by MIMCO/ICCA during the first round of audits in 1999. The plant management has consistently resisted making changes, although it involved no additional costs. Instead, it argued that since all workers left at the same time at the end of their respective shifts, it is easier for the supervisors to log-in the time for all workers and that individual clock-out was not necessary. Finally, in the post-audit meeting in April 2008, Mattel agreed that the plants would change their clock-out policies and that all clocked employees would have their checkout times recorded in the computerized records. However, ICCA has no further information since Mattel has cancelled its program of independent external audits.

**Malaysia**

At the time of the first audit round in February 8–10, 1999, Mattel had four plants in Malaysia. Since then Mattel has closed two plants due to changes in demand for its products and resultant downsizing of its worldwide production facilities. The remaining plants were Mattel (Malaysia) Sdn. Bhd. (MMSB), and Mattel Tools Sdn. BHD. (MTSB). In addition to the first round audit, the two plants also underwent full-fledged formal audits in May 2002, April 2005, and April 2008.

*MMSB*

This plant is a dedicated facility for the production of “Hot Wheels” toy cars. It employs approximately 3500 workers on a year-round basis with additional workers added during peak production periods. MMSB’s workforce is unusual among Mattel’s plants in that it tends to be somewhat older, more mature, and with longer tenure of employment. Average age of workers is 28 years and the average length of employment is 13 years. For 40% of the interviewed employees, this was their first job.

MMSB also participates in Malaysia’s guest worker program, which is supervised by the Malaysian government. The plant hires guest workers, exclusively from Indonesia, via recruitment agencies. At the time of 2008 audit, there were over 800 such workers comprising 29% of the direct labor workforce.

The MMSB plant is a well-maintained physical facility and provides a safe and comfortable working environment for its workers. Overall, workers have indicated a high level of satisfaction with the safety and quality of their work environment. The plant safety and maintenance conditions were also confirmed by the MIMCO/ICCA audit team of experts through an extensive “walk-through” of the plant facilities and review of the company’s records with regard to environment, and health and safety requirements stipulated in the GMP in all three audits in 2002, 2005, and 2008.

Malaysia has no minimum wage requirements. MMSB pays market-based competitive wages that are also in full compliance with Mattel’s GMP Standards. An overwhelming number of workers interviewed by MIMCO/ICCA during its four audit rounds expressed satisfaction with wages, benefits, working hours, and in the way they were treated by the management. There were, however, some complaints expressed by the workers during one-on-one confidential interviews (2008 audit) about pressure from supervisors to work overtime when an employee was unwilling to do so.

With regard to maintaining electronic time record, MMSB follows a similar practice that was criticized by MIMCO/ICCA in the case of Indonesian plants, i.e., workers swipe their magnetic card while coming into the factory, but do not clock-out upon completing their shift. Just as in the case of Indonesian plants, the plant management’s



arguments in support of this practice were equally untenable and spurious.

MMSB houses a very good clinic with four beds, which is staffed with three nurses (one State Enrolled nurse and two State Registered nurses) (RNs) based on one RN per shift. There is no charge for medical services or medicines provided to workers. The plant operates two canteens accommodating approximately 1800 workers per day. The plant pays the workers a food allowance of RM 3.2 per day. Cost of food at the factory's canteens is approximately RM 2–2.5. Workers who bring their food from home are entitled to the bi-weekly paid meal allowance.

At MMSB, the dormitories and living conditions are perhaps the best, home like, and pleasant, than any other facility visited by MIMCO/ICCA. In terms of the density in living space, and in relative level of comfort, these facilities provide a very good inspirational benchmark. At MMSB, all single-female female workers live in the dormitories. MMSB management considers it necessary for the safety and security of workers. Among the interviewed workers, employee satisfaction with various elements of dormitories and living accommodation ranged between 91 and 100%. In informal discussions with workers during MIMCO/ICCA's visit to the dormitories, workers expressed tremendous pride in their living accommodations. These dormitories generally meet and exceed all pertinent GMP standards.

MMSB has a handicapped worker program that deserves special mention. Under this program, MMSB hires and trains blind workers and places them in regular assembly line jobs. During the walk-through of the plant, MIMCO/ICCA members had the opportunity to observe these workers at their workstations and talk to them about their work experience. Without exception, these workers appeared happy and proud of their work. We also noted that there was no difference in the production efficiency and safety levels of these and other plant workers.

#### *MDT*

This audit report covers two plant sites used by Mattel's development and tooling operations in Malaysia. The first facility called Mattel Tools Sbn.

Bhd. (MTSB) was audited in February 1999, May 2002, and April 2005, when it was renamed as Mattel Development Tooling Sbn. Bhd (MDT). The plant is located in the Prai Free Trade Zone area outside Penang, Malaysia. It is a tool and dies manufacturer, which supports Mattel plants worldwide. The last audit was conducted on April 23, 2008 at a new site, which was also located in the Prai Free Trade Zone area.

The plant employs around 180 workers. Of these approximately 75% are direct labor (manufacturing) and the remaining 25% are professional administrative and clerical personnel. The workforce consists of highly skilled technicians, and professionally trained tool and die makers. Turnover among regular workers is quite low with the average work tenure at the plant of 13 years. The gender composition of the workforce is 93% male.

MTSB is an efficiently laid out and well-managed plant facility. It is completely air-conditioned. The factory maintains detailed and up-to-date records on plant maintenance, air filtration system, noise control, fire prevention, and safe storage and handling of hazardous materials. The facility has satisfactory compliance with GMP requirements.

Workers at MDT receive wages far exceeding market rates for hourly workers. There is an extensive and formalized communication system, which facilitates two-way communications between the employees and different levels of management. Workers were almost unanimous in stating that they would seek advice on personal problems from the line leaders or supervisors.

MDT shares a clinic with MMSB and all workers have full access to these facilities. MDT keeps first aid boxes on its premises for immediate first aid treatment. There is no charge for medical services or medicines provided to workers. Food in the factory canteen is provided by a contracted caterer. Costs are subsidized by the factory and average RM 1.5–3.5, (USD 0.39–0.92) paid in cash, per meal. The canteen serves four meals a day throughout all shifts.

The last audit of the MDT was conducted at the factory's new site. ICCA's overall observations with regard to MDT's practices at the new site were quite satisfactory. MDT has clearly established policies and rules with regard to verbal or physical abuse, including sexual harassment. However, in practice, these rules did not appear to be effectively

implemented. During ICCA's confidential one-on-one interviews with workers, almost 40% of the interviewed workers felt that there was favoritism and unfair treatment in employee appraisal for promotion and assignment for overtime work. In response, plant management provided a detailed plan of action. Follow-up inquiries by MIMCO/ICCA indicated that the issues were largely resolved.

A major point of contention in the case of MDT is the factory's practice with regard to maintaining time records, identical to the one described in the case of other plants in Indonesia and Malaysia. Unfortunately, the responses by the plant management are similarly untenable.

### Thailand

MIMCO/ICCA has conducted four formal audits of Mattel's only plant in Thailand, MBK in April 1999, May 2002, April 2005, and April 2008. The plant is located in the Bangpoo Industrial Estate Export Zone in Samutprakam outside Bangkok. It is a wholly owned Mattel facility and is dedicated to the exclusive production of Hot Wheels™ brand toy cars. The factory is capable of producing 100 million hot wheels cars a year.

Employment at MBK has ranged between 1350 and 1400 workers. Of these, 80% are direct labor while the remaining 20% comprised clerical, administrative, and supervisory staff. Almost 98% of the workforce is female. The entire workforce is over 18-year-old, and the average age is 29. The level of education of the workers employed by the plant is relatively low and averages between 6 and 7 years of formal education, which is equivalent to slightly above primary school.

Throughout the four audits MIMCO/ICCA found the plant facilities maintenance and upkeep to be excellent and in full compliance with the Thailand government regulations and Mattel's GMP standards. MBK maintains up-to-date records with all aspects of plant operations and management. The "walk-through" inspection of the plant showed the factory to be in good operating condition. All work areas were clean and free of oil spills and litter. MIMCO/ICCA also noted, where applicable, employees were using the proper personal protective equipment (PPE) in all areas of the operation. The

usage of PPE appeared to be strictly enforced by floor supervisors.

A recurring theme of discord among the workers has been excessive heat in the factory as the plant is not air-conditioned. The factory has launched a major effort to reduce plant temperatures and increase air circulation. The plant was being modified by changing the configuration of ceilings, walls and location of plant functions and other heat reduction technologies such as air curtains at certain workstations. It is expected that when all the construction work is completed the temperatures should decrease by 3–5°C.

MBK's wages and benefits policies as well as regular and overtime hours comply with Thailand laws and GMP standards. ICCA's examination of factory's payroll records confirmed the accuracy of appropriate payments for the workers.

MBK employees are represented by a union whose membership is voluntary. There is a standing union committee, which is responsible for facilitating daily communications between workers and plant management. Union leadership is elected annually by the plant's workers. Employees have unhindered access to top management. MBK senior management organizes regular plant-wide meetings.

MBK has installed computerized management systems to ensure that each employee's work hours conform to Mattel's GMP. This system checks every day's work schedule to make sure that they comply with GMP provisions. MBK also practices not swiping cards for time-out record keeping which is similar to other Mattel-owned plants in Indonesia and Malaysia. ICCA has already noted its objections. The situation defies rational explanation and remains a mystery to ICCA.

The plant houses a good clinic with five beds, staffed by a doctor and a State Enrolled Nurse (RN). The majority of injuries and sicknesses are burns, cuts, and respiratory problems. There is no charge for the medical services or medicines provided to workers. Employees are given annual health examinations free of charge.

MBK has no on-site residential facilities. All workers live at home or make their own living arrangements. MBK subsidizes 47% of the cost of the meals. The kitchen and canteen are well lit and clean. The factory kitchen and canteen can serve three meals a day to all workers. All food handlers

are required to have an annual physical check-up. In addition, workers may purchase other food items from any of the five shops selling a variety of food products.

MBK is been one of the best Mattel-owned and operated plants audited by MIMCO/ICCA. The plant has a stable cadre of senior managers who appear committed to operating a well-maintained and smoothly functioning plant. The management has also demonstrated a strong commitment to creating a worker friendly work environment.

## China

### *Mattel-owned and operated plants*

ICCA conducted three rounds of formal audits of the four Mattel-owned and operated plants in China. The first two plants are Chang An (CA) also known as Meitai, and Guan Yao (GY) also known as Zhongmei. Both are large factories with each employing between eight and nine thousand workers during peak production periods and are dedicated to the manufacture of Barbie dolls and related toys. The third plant is Mattel Die Cast (MDC), a medium-sized facility manufacturing die-cast toys, which employs between 1000 and 2500 workers and is located near the GY plant. In 2006, it was re-tooled to include plastic toys in its manufacturing portfolio. Workers in all three facilities are mostly young, female workers.

The fourth plant, Mattel Engineering China (MEC), employing about 350–400 workers, mostly male and trained, professional technicians and engineers, is dedicated to the manufacturing and repairing of the tools and dies used in other Mattel plants worldwide.

Mattel's manufacturing arrangement in China is based on a processing fee agreement with its local partners, who are government-controlled entities. In this business model, the local partner owns the facilities and employs the workforce while Mattel provides raw materials, equipment, and manufacturing engineering advice. The local partner is compensated by Mattel based on production volume. While the final authority and responsibility lies with the local partner<sup>4</sup> in matters concerning worker

rights, safety, and treatment, it should be noted that the sole purpose of these facilities' founding and existence is to build Mattel toys for export.

ICCA conducted three rounds of formal audits of Mattel's China plants in 1999,<sup>5</sup> 2003, and 2007. They also involved several follow-up visits to all four facilities through mid-2008. The purpose of the follow-up visits was to evaluate the effectiveness of corrective action plans submitted by Mattel to ICCA. All these reports are made public and available on Mattel and ICCA websites.

Guan Yao and Chang An – the two plants accounting for a majority of the workers – turned out to be the Achilles Heel through the entire duration of ICCA's audit life cycle. From the very start, ICCA had serious questions about the practices in these plants with regard to proper compensation of workers as mandated in China labor laws and GMP standards. There were similar questions with regard to legally mandated benefits, e.g., maternity leave and annual leave, deductions for dormitory rent, charges for food, etc. These issues continued to be challenging through the entire duration of ICCA's involvement.

The process, however, turned out to be that of a wave effect showing ebbs and flows but in the end, nothing much changed. From the very start, MIMCO/ICCA audits reported serious violations of GMP standards and China law. In the early stages of the audit process, Mattel's internal group followed through on ICCA's findings with continued inspections and advice to the plant's management for improved compliance efforts. Initially, Mattel's response to ICCA's findings was quite proactive even when it involved a significant cost in forms of capital improvements. For example, during the initial audit, ICCA found a dormitory in such poor condition that it was almost uninhabitable. However, the plant's China partner argued that since the dormitory was built long before the introduction of GMP, it should be exempted from GMP standards. This was an untenable argument and was rejected by ICCA. For Mattel's top management, this situation was equally unacceptable. Consequently, Mattel took the responsibility for rehabilitating the dormitory. The improvements, mostly in the female workers' living conditions, were so significant that it moved the Asia Regional Manager for Mattel to comment as to the tremendous difference this audit

had made to the lives of current and future workers at the plant.

Unfortunately, ICCA's experience with other issues identified in the audit was not so encouraging. As details in the following sections indicate, a majority of other GMP non-compliance issues – both substantial and routine – remained unresolved. In every formal audit or its follow-up, either new or equally blatant practices were observed or old ones had resurfaced. Shortly after ICCA's last audit in 2008, Mattel indicated that it would pay for some of the important changes in the plants' accounting and record-keeping systems that were at the core of opaque reporting of workers' wages, working hours, and working conditions. However, before these changes could be monitored and confirmed, Mattel decided to discontinue its independent external monitoring program.

While Mattel's responses toward mediation were well intentioned and earnest, they were quite often unsuccessful. It was apparent that Mattel's China partners were unwilling to make changes in their record-keeping practices that would result in greater transparency. There was also strong resistance to making any changes that would incur additional costs, which China partners were unwilling to undertake. From ICCA's perspective, the China partners at the two plants viewed GMP as something that belonged solely to Mattel and for Mattel to pay for its implementation. However, it was not clear that even if Mattel had agreed to pay for the necessary changes that China partners would be willing to go along.

### *Audit findings*

#### *GMP awareness*

A serious issue of concern at the start of the monitoring program was workers' awareness of Mattel's GMP initiative. Without proper awareness of the underlying principles, it would not be meaningful to expect or monitor compliance. ICCA interviews revealed that orientation programs and periodic communication protocols did not succeed in this area, with the exception of MDC, which showed that 87% of workers were aware of the GMP. Management concurred with ICCA's findings and promised to take appropriate steps to ensure all

workers' GMP awareness. Follow-up audits of CA and GY revealed that a good-faith effort was in place and ICCA was convinced that the situation would be remedied in a sustainable manner in the future.

The second round of audits noted that while the smaller MDC and MEC plants sustained their workers' GMP awareness, GY and CA, the two plants with the largest number of workers had not made noticeable progress. By the time of the third round of audits only 30% of GY and CA plant workers were aware of GMP.

#### *Working hours*

The extent of maximum allowable work hours had been the most vexing problem that ICCA had encountered in its monitoring program in China. The initial audit of CA and GY plants, in 1999, encountered problems in the transparency and clarity of payroll records. As a result, it was not possible to make a determination as to the accuracy of working hours and wage payments because of the opaqueness of the factories' record-keeping practices. The situation was also exacerbated by the confusion among workers with regard to their understanding of the pay stubs and their inability to verify their wages. Following the audit, Mattel and ICCA reached an understanding that the payroll systems would be re-designed for transparency, and that ICCA would revisit these plants within 1 year to verify the compliance of new systems. There were no payroll-related problems encountered in the MDC and MEC plants during the first round of audits.

ICCA's second round of audits in 2003 found all Mattel plants to have circumvented the spirit of GMP via the use of several local variances, which allowed them to exceed nationally mandated work hours limits. These included: *Consolidated Hours* which allowed a plant to schedule the total permissible yearly overtime hours (36 h per month for 12 months) during a shorter time span; *Extended Hours Permit* which allows plants to schedule 60-h workweeks throughout the year; *Peak-Season extended Hours Permit* which allows plants to schedule custom-tailored work schedules based on their self-stated needs. All four Mattel plants had secured these three permits, albeit without the locally required stipulations about their duration, and specific daily, weekly limits. ICCA expressed concern over these

practices, recognizing them to be *carte-blanche* for unfettered management liberties at the expense of the workforce. This observation was also accompanied by a formal request from Mattel to take a clear stand on this issue and establish standards to which these plants would adhere.

In 2006, Mattel responded by allowing for a maximum of 12-h workdays and 60 to 72-h workweeks, where such weeks would be limited to 17 per year. Furthermore, no worker would work in excess of 13 consecutive workdays, ensuring at least one rest day per week. Even though similar practices were the norm in the region, this policy was in violation of the Chinese labor law, as acknowledged by Mattel.

ICCA's 2007 audit found all four plants to exceed the 12-h workday and 72-h workweek standards as well as the 17-week limit on 60 to 72-h workweeks. ICCA concluded that all applicable laws, permits and standards, self-imposed, or otherwise, had been entirely meaningless throughout 9 years of the monitoring program.

CA and GY had also created an arbitrary set of rules denying workers overtime pay when they had exceeded their regular hours work schedule rates while workers were required to be on premises in CA and GY plants. CA did not pay overtime wages to line leaders for a maximum of 2 h per day even though their workday may extend beyond 10 h per day. MDC did not pay overtime wage if less than 30 min per day or if daily overtime exceeded 3.67 h per day; workers were given time-off on other days, but were compensated at regular wage rates. ICCA requested that Mattel pay back wages to those who were not paid at their entitled rates. Somewhat similar, although less severe, problems were identified in MDC's record-keeping system, which resulted in workers being compensated based on established production schedules rather than their time card records.

#### *Benefits and deductions*

Contrary to the provisions of the Chinese labor law, which allows for 90 days paid maternity leave, GY, CA, and MEC plants were not extending any benefits to their workers at the time of the first round of audits. Upon ICCA's observations of this issue, the second round of audits noted some policy revisions: GY allowed 1 month paid leave with 3-year tenure;

CA allowed 45 days paid leave to staff and was planning to extend 90 days paid leave to all workers in 2001. MEC and MDC complied with the law and Mattel's GMP regarding this issue. The second round in 2003 revealed that GY and CA had implemented their stated plans, and that MDC was paying the benefit upon the workers' return, thus denying those who resign their entitled benefits. The third round of audits conducted in 2007 found no changes in the plants' respective policies.

With regard to annual leave policies, three of the four plants had been compliant with GMP standards starting with the first round of audits; CA had no annual leave benefits in 1999, and had planned to offer 1 week paid leave to staff in 2001, extending it to all workers in 2002. The 2003 audit observed that the annual leave was offered only in December (coinciding with factory closures leading to, and through the Chinese New Year), and any worker who resigned before then would forego their benefits even if they were entitled. This policy was changed to conform to GMP standards by 2007.

ICCA recognized that all plants made considerable progress in meeting their obligations through the third round of audits in 2007. Nevertheless, it noted its disappointment that such apparent violations with the resultant loss of income for the workers should take so long to remedy in Mattel's China plants.

Most workers in Southeast China come from other provinces as guest workers. They also tend to stay in the dormitories and eat in the cafeterias provided by the factories. Chinese labor law allows dorm and food charges to be deducted from the workers' paychecks, but not to exceed 50% of the monthly minimum wage for the district. ICCA's first round of audits found no irregularities with respect to deductions applied to workers' earnings. MDC had a noteworthy policy of providing free food to all its workers during their employment. However, during the second round in 2003, CA and GY plants were found to be charging in excess of the 50% of minimum wage, which was also the standard established by Mattel under GMP. The third round of audits also noted a predatory policy on the part of CA management, which required workers to opt in or out of the dorm and meal plans for the duration of their contract. For guest workers in the province, and mostly first time employees, the practical impact of this policy was to have 100% of the workforce on



mandatory meal plans regardless of whether or not they ate at the company canteens.

*Environment protection, and worker health and safety issues*

Mattel's China plants and notably Chang An and Guan Yao plants, were equally lagging in their compliance efforts, and reticent about providing information with regard to these activities. Looking back, the emerging theme through ICCA's monitoring span of 9 years is that the Chinese plants had not followed through with the environmental, health and safety measures they had initially undertaken to comply with Mattel's GMP. Although, the plants had started monitoring programs with commendable efforts in terms of ensuring worker safety and environmental consciousness, over the years, these efforts had given way to a managerial attitude of "getting away with investing as little as possible, while maintaining compliance with the bare minimum standards." Predictably, and unfortunately, instead of the "continuous improvement" culture, which ICCA had signed on to facilitate, this approach resulted in a continued deterioration of plants, facilities, equipment, and ultimately, worker safety.

### **Mattel's China vendor plants**

Mattel outsources approximately one-half of its production needs to about 40 major vendors in China. Over the period of 2000–2008, ICCA audited 20 top vendor plants. These factories represented approximately 75% of the total procurement of Mattel's third party manufacturing in terms of dollar value. These are top tier vendors, and in a number of cases, these plants are solely dedicated to the production of Mattel-branded toys. All of the production facilities are located in Guangdong Province in South China, and offer employment to between 70,000 and 100,000 workers depending on the production cycle.

The compliance requirements for the vendor plants are set up at a somewhat lower level compared to the company-owned and operated plants. Nevertheless, they stipulate compliance with legal requirements as a minimum for acceptable performance.

ICCA's work with Mattel China vendor plants started in 2000–2002 with a series of initial vendor consultation visits. These consultations were aimed

toward developing a better understanding of the prevailing operating conditions in the supplier plants and their impact on employees' working and living conditions. The findings provided a mixed picture of the vendors' performance (Sethi et al., 2000). In one sense, this was to be expected considering the overall low level of environmental and social performance in locally owned and managed plants. Both Mattel and ICCA anticipated that moving these plants forward would demonstrate significant improvement in their GMP compliance. There was also the implied expectation that all else being equal, Mattel would reward these plants with additional business.

*First round of China vendor audits 2002–2003*

The first round of formal audits of China vendors was conducted in August 2002 and January 2003. It covered 12 of the 20 plants that ICCA audited throughout the program, and comprised approximately 50% of Mattel's procurement budget from China vendors. As a matter of commercial non-disclosure agreement, all audited plants have been assigned a number (e.g., Plant 1, Plant 2, etc.) and are referred to by the corresponding number in all Mattel's and ICCA's documentation (Exhibit 4).

Exhibit 4: Characteristics of plants

| China vendor<br>Plants no. | Number of<br>employees<br>Regular peak | Capacity<br>dedicated to<br>Mattel products |
|----------------------------|--|---|
| Plant 1                    | 3700                                   | 60%   |
| Plant 2                    | 1100                                   | 100%  |
| Plant 3                    | 1700                                   | 85%   |
| Plant 4                    | 1250                                   | 70%   |
| Plant 5                    | 9200                                   | 60%   |
| Plant 6                    | 8100                                   | 60%   |
| Plant 7                    | 7800                                   | 20%   |
| Plant 8                    | 6200                                   | 40%   |
| Plant 9                    | 3500                                   | 40%   |
| Plant 10                   | 5800                                   | 60%   |
| Plant 11                   | 1400                                   | 80%   |
| Plant 12                   | 4500                                   | 100%  |
| Plant 18                   | 4200                                   | Not available                               |
| Plant 17                   | 4200                                   | Not available                               |
| Plant 21                   | 2200                                   | Not available                               |
| Plant 15                   | 2400                                   | Not available                               |
| Plant 14                   | 8500                                   | 45%   |

Exhibit 4 continued

| China vendor<br>Plants no. | Number of<br>employees<br>Regular peak | Capacity<br>dedicated to<br>Mattel products |
|----------------------------|--|---|
| Smile                      | Not available                          | Not available                               |
| Plant 13                   | 4000                                   | 50%   |
| Plant 16                   | 4600                                   | Not available                               |
| Plant 19                   | 2500                                   | Not available                               |
| Plant 20                   | 1900                                   | Not Available                               |
| Plant 21                   | 2000                                   | Not available                               |

The findings of the audit revealed a number of areas where substantial improvements had been achieved since the consultation visits. They also indicated that more work needed to be done in general maintenance of the facilities as well as in treatment of workers. The audit established that there were no under-age workers employed in any of the audited vendor plants. Vendor plants were paying appropriate wages for regular and overtime working hours. There were also noticeable improvements in health and safety standards although from a very low starting point.

Dormitories and canteen facilities were a mixed bag. In part, it reflected the unusual situation wherein a unit of the local government built and operated dormitories to meet the needs of a cluster of factories. The situation created a conflict of incentives and split responsibility. The dormitory owner sought to maximize its profit margin by building poor quality dormitories and skimping on maintenance and upkeep. Factory owners did not have enough influence on the dormitory providers to improve cleanliness and maintenance. Instead, some unscrupulous factory owners sought to earn extra revenue from the difference in the rent they charged to the workers and their actual costs.

The record keeping for work hours also showed improvement from the conditions observed by ICCA during the initial round of informal fact-finding visits. A major area of persistent non-compliance pertained to the maximum numbers of hours worked, which invariably exceeded the legally mandated standards and even somewhat relaxed standards in the GMP.

The problem of excessive work hours had three dimensions, which made it all but impossible to

comply with any of the legal or other standards, e.g., GMP.

1. Factory owners were strongly motivated to get contracts from foreign buyers with promises of on-time delivery, which would be impossible without resorting to work weeks of 68–72 and more hours.
2. While foreign buyers made public display of their anguish about excessive working hours, there was no planning to create timely order flow keeping in mind the plant capacity and total labor available. This was equally true in the factories that were completely dedicated to manufacturing goods for a single buyer, in which case the buyer (a) had to be fully aware of the number of work hours/workers that would be needed to fill the order and (b) had total control over the production process to restrict excessive hours.
3. In a majority of cases, workers themselves were interested in working long hours to earn more money from a meager base to both support themselves while working, and to save money for their families left behind in their hometowns and villages. Therefore, they would leave factories that did not provide work for lots of overtime hours.
4. To avoid problems with foreign buyers, factory owners often resorted to a variety of accounting and bookkeeping tricks to create superficial records to show compliance with laws or voluntary code standards with regard to regular and overtime working hours, and payment of appropriate wages for those hours.

From this step, it was not too difficult for some unscrupulous factory owners to use similar tactics and thus underpay their workers for any work done. Some vendors also manipulated wage calculations by creating parallel system of piece rate (which was hard to calculate and poorly understood by the workers) and hourly rates (as required by the law) and thereby making the system complex and opaque, which invariably benefited the factory owner at the expense of the workers.

During its various audits, it was observed that Mattel had to deal with the reality of the marketplace and allow for working hours that exceeded

legal limits of maximum hours. Nevertheless, Mattel succeeded in (a) maintaining a transparent and fully verifiable system of time records, and even more important (b) ensuring that workers received appropriate wages for the number of regular and overtime hours worked. Furthermore, Mattel's auditors were substantially successful in keeping to minimum, and within reasonable limits, the deductions from workers' wages for such items as dormitory rent, cost of food, uniforms, medical charges, cash fines for various work-related infractions, etc. It was a continuing source of concern to Mattel and ICCA since local factory owners were quite inventive in finding new deductions that could be imposed on the workers. It should also be noted that Mattel was quite reluctant to use its strongest weapon, or even threaten to do so, namely, to drop a factory from its supplier pool.

The situation with regard to plant maintenance and prevention of contamination of air, ground, and water resources has improved over the audit life cycle, although there was considerable divergence among different plants. In general, most of the factories were responsive to changes that would improve overall routine maintenance of plant and physical facilities, which were also conducive to improving working conditions for the workers. However, when it came to major equipment, purchases, e.g., water treatment for paint removal, air circulation systems, etc., there was considerable resistance because the equipment required capital expenditures that could not be directly related to increased production. There was also the issue of lax regulatory oversight, which further reduced any pressure toward making needed improvements. A third element had to do with lack of trained and experienced personnel. In a number of cases, ICCA observed that the factory had excellent equipment but it was inoperable because of improper installation and poor upkeep. Areas showing significant improvement included safety of workplace, dormitories and canteens, workers' access to all levels of management, discrimination or promotion based on sex, race or ethnic origins, and, significant reduction in poor treatment of workers.

Most plants demonstrated increased attention and concern for environmental issues both as they affected the workers inside the plant facilities, and as the plants' air emissions, water discharge, and waste

treatment affected the surrounding areas. However, overall upkeep as well as certain EHS aspects needed further improvements.

#### *Working hours*

At the time of the first formal audit of vendor plants, Mattel's GMP did not have any adjustments in its requirement for overtime hours that would address variations in seasonal production. Instead, it restricted the workweek to a maximum of 60 h, including overtime. ICCA's audit of the 12 vendors visited during the first formal visit showed that all of the vendors were routinely scheduling work hours that were in excess of the 60 h per week limit stipulated in the GMP, generally scheduling 66–72 h workweeks based on a 6-day workweek.

Furthermore, in a number of cases, the Consolidated Work Hours permits provided by local labor bureaus were so outside the prevailing norms as to question their authenticity. For example, the local authorization permits received by Plants 10 and 11 included an authorization to exceed the maximum annual overtime hours provided under the Chinese labor law. ICCA had found no other instance of similar extension in its audit work in China. The permits for Plants 11 and 12 allowed them to work 1040 overtime hours during 2002, extending the national China labor law limit of 432 overtime hours by almost 250%.

Mattel's GMP requirements obliged factories to provide workers with a compensatory day-off within 30 days for work scheduled beyond 7 consecutive days. Where a compensatory time-off day is not provided within 30 days, workers must be compensated at 2.0 times the normal wage rates. Of the 12 plants audited, five plants (3, 6, 7, 9, and 11), representing 23,000 workers, or 43.4% of the total workers covered in the audit, were unable to provide any records to show that they either provided an alternate rest day within 30 days or compensated their workers with double wages as required by the GMP standards.

#### *Mandatory overtime*

Both China labor law and Mattel's GMP require that all overtime work must be voluntary and that workers had the right to decline overtime work. In reality, a large part of overtime is mandatory and built into the workers' employment expectations.

This is a common practice and is accepted by workers. Therefore, from the perspective of the workers, the issue of involuntary overtime arises where (a) the implied consent as discussed above does not apply, and (b) a worker's request to be excused from overtime work because of tiredness, feeling ill, or other personal reasons has been denied. For example, in the case of Plant 1, management required that a worker must find a substitute replacement before he/she is allowed to decline overtime work. Similarly, some plants limited the number of workers who could refuse mandatory overtime (Plants 5 and 6). A particularly serious non-compliance of voluntary overtime policy was discovered by ICCA at Plant 12, where the entire workforce of 4600 workers was asked to work on a national holiday.

#### *Appropriate payment of wages*

While the payment of minimum wages and compensation for overtime hours improved since initial informal assessment, many plants were found to be involved in questionable practices involving monetary deductions from workers wages. One such area included imposition of cash fines as a disciplinary measure. Cash fines were found to be imposed by five factories (Plants 1, 5, 6, 11, and 12) representing 50% of the workers covered in the audit. It should be noted here that the imposition of cash fines is permissible under Mattel's GMP, which restricts cash fines to no more than 20% of the legal minimum monthly wage. Although individual fines imposed by the plants did not exceed the maximum limit provided in GMP, the frequency with which these fines were imposed, the total amount of funds raised by the plants' management through fines, and the disposition of these funds raised questions as to their effectiveness and utility. Vendors generally indicated that funds collected through cash fines were used for employee welfare activities including holiday celebrations and other entertainment programs. The factory managers' assertions in all these plants, however, could not be verified because the plants failed to provide any information or financial records to show how these funds were expended.

#### *Deductions*

Another area pertaining to monetary deductions involved charges for dormitory accommodations and

food served at the factories' canteens. Plants 8 and 9 required workers to make an upfront, non-refundable payment of RMB80 as the cost of initial supplies for dormitory living, such as bed sheets, towel, etc. Plants 1 and 11 also imposed a mandatory monthly fee charge regardless of where a worker lived. Plants 7 and 11 imposed mandatory deduction for food from workers' paychecks, regardless of whether or not they ate in the canteen. In Plant 1, eating in the canteen was mandatory. In Plant 8, although eating in the canteen was voluntary, many workers were not aware of it and ended up paying for it through mandatory deductions.

#### *Record keeping*

Areas needing improvement included record keeping of rest day work receiving either double wages or a compensatory day-off; inconsistent application of regulations with regard to fringe benefits, e.g., maternity leave, annual leave, use of cash fines; and, worker training with regard to safety, and inadequate use of personal protective equipment.

#### *Environmental protection issues*

Most noteworthy issues that surfaced were inadequate attention to macro, environmental issues, e.g., treatment and disposal of wastewater, air and water quality, ventilation, and a culture of inadequate attention to general plant maintenance and operations. Most factories were in non-compliance in varying degrees to GMP standards pertaining to environmental issues.

#### *Mattel's response*

In response to ICCA findings, Mattel provided details of its remedial action. The company's internal auditors analyzed over 300 specific findings from ICCA reports pertaining to the 12 plants. They worked with individual vendors to develop plans for corrective action to address the initial audit findings. The company provided ICCA with a detailed report showing how each change was organized and implemented with a record of verification and, where appropriate, provided for ICCA's review, copies of proper certification from appropriate government agencies and professional bodies. The company also provided photographic evidence of

new and repaired installations indicating the extent and scope of corrective measures taken by the vendors in cooperation with Mattel. As a result, of the 12 plants in the original audit, ICCA undertook a follow-up audit of the seven plants (Plants 1, 2, 3, 6, 9, 10, and 12) to verify the adequacy of compliance efforts. The follow-up audit indicated that with the exception of two plants (Plants 1 and 12), all plants were in full compliance with the GMP standards. The improvement of vendor plants performance since the initial visits, and Mattel's robust corrective action in response to ICCA findings marked substantial progress in China vendor plants' management and oversight.

#### *China vendor audits 2004–2007*

Over the period of 2004–2007, ICCA undertook formal field audits of nine additional plants as well as follow-up visits to the vendor plants that were found to be at various levels of violation of Mattel GMP. The audits revealed that the plants were generally in compliance with the main provisions of Mattel's GMP that were considered to be "zero tolerance" issues, e.g., child labor, forced labor, minimum wage, and discrimination at hiring.

Nevertheless, a number of questionable practices were discovered in relation to plant upkeep, use of PPE, workers' access to bathroom facilities and drinking water, and monetary deductions. Most common practices included charging workers for a medical examination required upon hiring, additional sets of uniforms, factory IDs, and offering maternity payment for workers only if returned to the factory after 90 days of leave. The issue of extended overtime continued to be a general practice at most of the plants. However, management had improved its compliance with securing Consolidated Work Hours permits, and violations in the overtime scheduling, although occurring in some instances, were no longer found to be a routine issue.

Another disturbing practice found at China vendor plants had to do with the plant management coaching of production workers in order to "pass" the inspection. In ICCA's audit practice, such incidents happened twice: in Plant 18 during initial formal audit in 2005 and in Plant 1 during its second formal audit in 2008.

Although Mattel management and its internal audit department continued to cooperate with the ICCA audit team in examining areas of compliance concerns and assuring ICCA in taking remediation, the changes in vendor plants' operations did not address all key findings, and in many cases included only policy and documentation improvements. ICCA's follow-up visits found numerous instances of continuous violation of maternity leave policies as well as persistent workers' complaints on inadequate access to bathrooms and drinking water during production hours. This situation is particularly troublesome, as improvement of workstation leave permits or payment of benefits should not pose any capital or operational burden on the plant management.

ICCA's first round of audits and follow-ups noted that both the vendors and Mattel internal audits had emphasized worker-related issues, i.e., employment of underage workers, excessive work hours, poor record keeping, and payment of improper wages for regular and overtime work. This was to be expected since these issues were closely identified with allegations of sweatshops. ICCA's audit team strongly indicated that worker health and safety issues and environmental concerns dealing with air, water, and ground pollution were an integral part of GMP and China labor laws.

In this case, vendor responses and Mattel's efforts were mixed and uneven. In fairness, it should be noted that Mattel's China vendor plants did not represent a homogeneous picture. Some of the vendor facilities showed substantial progress in improving the physical work environment at the factories. For instance, Plants 19 and 20 had air conditioning systems installed in all production floors – a practice seldom seen among supplier plants. Moreover, these plants offered worker accommodations that were better than typical worker dormitories, both in terms of individual space and general upkeep.

At the same time, other factories continued to use obsolete and poorly maintained equipment for water treatment, sludge removal, and air ventilation, since corrective action in these areas required capital expenditures and additional staffs for maintenance and monitoring. The plants consider these expenses as non-essential given the low profit margins and highly competitive markets. Mattel's internal audit group was invariably in agreement with ICCA's findings



and made efforts to improve the situation. However, Mattel was unwilling or unable to insist that these plants make the necessary improvement as required by China's laws and Mattel's GMP standards.

Overall, the second and third round of vendor plant audits suggested a widening gap between instances of non-compliance with GMP standards and Mattel's promises and performance to improve compliance by the vendor plants. Finally, as a follow-up to ICCA's third round of audits, Mattel provided ICCA in late 2008 with details as to its proposed corrective action pertaining to the vendor plants. The actual implementation of these actions remains unknown to ICCA as Mattel has terminated its independent third party external audits.

#### *Mattel's reluctance to discipline recalcitrant vendor factories*

Unfortunately toward the end of second round of audits, it became apparent to ICCA that Mattel's enforcement of its GMP standards was losing momentum despite clear-cut violations and repeated promises of change. Several factories stood out in their below-average level of management of social issues and their inadequate response to Mattel's requirements for independent audit.

#### *The case of Plant 7*

One of these factories was Plant 7, which was inspected during the first round of China vendor plants audit. During the initial audit, Plant 7 was found to have significant non-compliance issues in the areas of payment of regular and overtime wages, excessive overtime hours, and poor record keeping with regard to working hours and wage payments to workers. Mattel informed ICCA that the company had decided to discontinue its business relationship with this vendor. However, Mattel subsequently informed ICCA that, for business reasons, it had continued its contractual relationship with this vendor.

As a result, ICCA continued to observe the plant's operations. This factory was revisited three more times over the period of 2005–2007. During these visits, ICCA identified a number of non-compliance issues, involving mandatory deductions for medical check-ups, recruitment fees, charges for uniforms and factory IDs, discrimination at hiring for pregnant

workers. One of the most persistent issues that ICCA brought to the attention of Mattel's internal audit department was the unavailability of a consistent computerized record-keeping system. The factory was found to have two sets of books to meet recording standards of two major clients. Moreover, workers' hours were recorded by line leaders. The lack of transparency with regard to double bookkeeping and manual record keeping was repeatedly brought to the plant management's attention by ICCA and was also noted by Mattel internal audit reports over the years of the factory's inspection, but to no avail.

Another persistent practice in Plant 7's operations was related to routine work on Sundays creating a perpetual work schedule with one rest day every 13 days (instead of 7 days). It also became apparent during ICCA's discussions that Plant 7's management had no plans to change its practices with regard to scheduling work hours that were in excess of the maximum permissible limit or other practices, e.g., work on rest days.

In its latest response to ICCA's findings on Plant 7's practices, Mattel noted that it would not "continue a relationship with a vendor that does not demonstrate a commitment to comply with GMP." However, ICCA does not have any information as to whether or not Mattel's business with Plant 7 has been terminated.

#### *The case of Plant 18*

The most egregious situation occurred in Plant 18. The first audit of this facility was intended to take place in December 2005 following informal plant consultation. However, the audit was terminated by ICCA after it became apparent that a large number of the workers were told not to come to work on the day of the audit. Other workers were identified as having been coached by the management to provide predetermined answers, which compromised the integrity of the audit process. Both Mattel and ICCA agreed that Plant 18 would be given an opportunity to undertake the necessary corrective action following which the plant would be formally audited by ICCA.

The second formal audit took place on July 10–11, 2006. The audit found a number of non-compliance issues in workers' treatment and general plant upkeep. However, during confidential one-on-one interviews with workers it became apparent that the management had again resorted to coaching

the entire workforce at the plant to give similar answers to questions that might be asked during one-on-one confidential interview sessions to ICCA's audit team. The inconsistency between management claims and workers responses posed serious concerns about the integrity of the already quite negative audit findings. The widespread violation of extended overtime hours permits, deteriorating physical conditions of the plant facilities and workers' amenities left little faith in management's ability and intent to make the necessary improvements in the management style and operational policies.

Mattel was disappointed with Plant 18's lack of improvement and indicated that it would not provide any new business to the plant until the management adequately addressed the compliance issues outlined by ICCA. Unfortunately, the third audit visit of Plant 18 in 2008 did not indicate any improvements in the plant's management of labor and environmental issues. The plant was found to be one of the biggest offenders on Mattel's GMP standards as well as China Labor Laws. However, ICCA did not receive a formal confirmation from Mattel as to its action with regard to Plant 18.

#### *Coaching of workers*

The third visit of Plant 1 coincided with ICCA's third audit of Plant 18. Plant 1 audit was terminated due to similar findings of workers' being coached and cutting the workforce more than twice on the day of the audit. Moreover, worker survey conducted at another facility visited at the same round of audits (Plant 11) revealed that coaching of workers prior to audits was a regular practice. Workers at Plant 11 stated that they usually received cash awards for responding to the auditors' questionnaires with the predetermined answers. While the workers at Plant 11 refrained from giving ICCA's team preset responses due to the confidential nature of the survey, their acknowledgment of such practices raises serious concerns about the integrity of independent audits conducted by various groups in China vendor plants.

#### **Concluding remarks: lessons learned and unlearned**

In this article, we have presented a detailed description and discussion of Mattel's voluntary code of

conduct, the circumstances that led to its creation; the process by which it was implemented, and ultimately abandoned by the company. The authors of the article were intimately involved in almost every aspect of the code creation and implementation throughout its entire life cycle of approximately 9 years.

This case study has offered us an invaluable opportunity to examine the dynamic nature of changes within the company and how they impact and are impacted by the changes in the company's external competitive and socio-political environment. Mattel's GMP was a highly innovative and one-of-its-kind initiative. In this sense, it became a live laboratory, however, imperfect, to examine various aspects of the viability of a voluntary code of conduct by companies and industry groups. To the extent that it provides a meaningful mechanism toward self-regulation that would be flexible and adaptable to changing economic and socio-political circumstances, it could also help to narrow, if not completely eliminate, the gap between societal expectations and corporate performance.

Ideally, it would have been desirable to examine similar cases of voluntary codes of conduct and follow them through the process of code creation and implementation over a certain length of time. Unfortunately, this has proved to be impossible. An extensive search of literature by the authors has failed to discover any instances of publicly reported voluntary codes of conduct. Notwithstanding the paucity of other comparable case studies, we believe our observations may suggest potential pathways, which companies and industries could put to good use in creating and implementing voluntary codes of conduct.

Our analysis in this section has been divided into four categories:

1. Corporate responses to external crises;
2. Importance of ethical norms, corporate culture, and institutional memory;
3. Operational aspects of implementing GMP; and
4. Corporate responses to competition, regulatory environment, and reputational risk.

#### *Corporate response to external crisis*

Why is it that companies in a given industry, when confronted with an external crisis, respond differently to similar situations? Our analysis in this

instance, and in a number of others examined by this author (Sethi and Williams, 2000), indicates that a large part of the differences can be traced, first, to the character and vision of the company's CEO and its top management. The innovative and potentially risky challenge of launching Mattel's GMP was the responsibility of Mattel's then CEO, Ms. Jill Barad. From all accounts, she was a highly focused and determined executive who would force the organization in a preferred direction by sheer force of personality. She spent a major part of her career as a marketing executive, and was very sensitive to public perceptions and risk to corporate reputation. In addition, she had the confidence and support of Mattel's board, which included a member of Mattel's founding family.

Ms. Barad saw the crisis in terms of public perception and reputational risk that would need a bold response to gain public confidence. In this assessment, she was quite right. Despite some skepticism, the GMP initiative received positive coverage in the news media and supportive comments from Mattel's critics and the NGO community concerned about sweatshops and human rights abuses. Therefore, from the very start, the top management was committed to the creation of GMP. While there were extensive discussions and differences of opinion, they focused on making the code work.

No sooner had the code been put into practice, there was a change in the top management. Ms. Barad's successor at Mattel was Mr. Robert A. Eckert, who also came with a background in marketing having previously served as the CEO of Kraft Foods, Inc. (Hays, 2000). The new CEO and his top management team found good reasons to be supportive of the GMP initiative. He offered strong endorsement based on his belief that companies must demonstrate responsible social conduct to legitimize the right of self-regulation. As we stated in an earlier part of this article, he further reiterated his belief in a speech at a United Nations conference (ICCA, 2007), and in comments to a reporter from the New York Times (Dee, 2007).

#### *Corporate culture and ethical norms*

Corporate culture, i.e., a company's institutional values and traditions, provide the glue that binds

companies' various internal constituencies into a cohesive community. It also serves as a filtering mechanism through which the company views its external environment. Without a supportive corporate culture (internal) and corporate reputation (external), the CEO and its top management team are likely to meet strong resistance from within and without when trying to impose discrete and substantive changes in corporate strategy and conduct. Similarly, a CEO who is not in synch with corporate culture and prevailing societal expectations, is unlikely to maximize the value of these resources. It will be difficult to create a viable strategy that the company's managers and employees will enthusiastically implement, and the company's stakeholders will accept.<sup>6</sup>

From our observations, and working with executives at various levels of the Mattel organization, we could not ascertain a discernible corporate culture that was unique and distinctive from the corporate culture prevailing among most large corporations, and more notably, large MNCs. In part, this may have been due to Mattel's turbulent corporate history where the company went through severe financial and strategic missteps that brought it to the brink of financial collapse. The latest change in corporate leadership at Mattel appears to be symptomatic of this trend. This culture can best be described as insular, focused on internal efficiencies, and where most other constituencies are viewed in transactional terms and bargaining leverage determines their relative value to the corporation.

From our perspective, the contemporary Mattel, Inc., is a company driven by economic and market considerations. Its business practices, apart from GMP, are no different from most other companies in the toy industry. When it comes to corporate social responsibility (CSR) and good corporate citizenship, the company uses it as a thin patina to wrap around its "business as usual" modus operandi. The primary intent of the GMP was to embed CSR and make it an integral part of corporate strategy and operations. This would transform the notion of CSR to corporate social accountability. It would imply that GMP-related activities would not be viewed as a reflection of good corporate citizenship, but as an integral part of managing reputational risk and maintaining a sustainable business model.

*Operational aspects of implementing Global Manufacturing Principles*

The initial response of Mattel's management to ICCA's audit findings was prompt and unambiguous. ICCA was encouraged to communicate directly with Mattel's top management. The president of ICCA was invited to speak at Mattel's Annual Shareholders meeting. At the operational level, Mattel's social audit department provided timely and systematic response to ICCA's findings, supervised corrective action at Mattel-owned and operated plants as well as vendor plants. Even more important, Mattel's top management supported ICCA by requiring major changes in its factories in Mexico and China.

Field operations received two types of signals as to top management's expectations with regard to GMP compliance. The first set consisted of formal communications that outlined lines of authority and responsibility for GMP compliance. These were reinforced through the regular meetings between top management and senior managers from the field. Equally important were the signals that were sent by top management's actions such as the rehabilitation of factories in Mexico and China.

The progress in GMP compliance during the first 4 years was impressive and universal. Under the circumstances, it would be logical to assume that top management expectations with regard to GMP would be integrated in business operations, management performance, and compensation. Unfortunately, in reality this expectation was not fully realized, and it set in motion a gradual erosion in Mattel's commitment to GMP principles and practices.

- (a) From the outset, Mattel had excluded its licensee operations from ICCA Audits. Financial analysts estimate that Mattel derives almost 50% of its total revenue from licensing operations. The exclusion of this activity would thereby significantly impact the company's overall attitude toward GMP. It will make licensing operations more profitable and less subject to public scrutiny when compared with revenues from Mattel's own manufacturing and procurement operations.
- (b) A similar situation existed between the company-owned and operated plants and

the vendor-owned plants. Managers of Mattel-owned plants often complained about Mattel's double standard whereby vendor plants were held to a lower standard of GMP compliance, which put Mattel's own plants at a competitive disadvantage when making similar products.

- (c) Among the vendor plants, ICCA also received comments that Mattel does not necessarily reward vendors having a higher level of GMP compliance with either bigger orders or higher prices to compensate for their GMP compliance costs.
- (d) As we have noted in earlier parts of this article, notwithstanding Mattel's formal commitments and assertions, the company was quite reluctant to discontinue its business relationships with vendors that were charged with repeated violations of GMP standards.
- (e) With regard to social audits and Mattel's GMP compliance efforts, the company's organizational structure and operational procedures created conflicting goals. The field level auditors, especially in China, had a direct line reporting to the area level managers who were also responsible for timely and cost effective procurement of toys.
- (f) ICCA's continuous interaction with Mattel's field operators suggested that area managers were happy to ensure GMP compliance where such compliance was easily accomplished, did not elicit resistance from the vendors, and would not disrupt the flow of products. This had the effect of many vendor plant managers and even Mattel's own plant manager to downgrade, if not ignore, recommendations of Mattel's own social compliance auditors.
- (g) ICCA found Mattel's social compliance auditors in the field to be highly experienced and dedicated to the task of improving GMP compliance, and where appropriate, helping vendor plant managers with advice and training. This was especially true in the case of China where conditions for improving GMP compliance were difficult and challenging. Nevertheless, Mattel's China-based social audit group frequently lost its

most experienced people because of the less rewarding work environment at Mattel and more remunerative career opportunities elsewhere.

- (h) The situation with regard to the social audit group at Mattel's headquarters was equally uncertain. Over the 9-year time span, ICCA noticed a high rate of turnover among its professional technical staff. The reasons for such turnover were also apparent and predictable. From ICCA's perspective, these professionals appeared not to be confident of the company's total commitment to GMP and thus found their work somewhat marginalized leading to poor job satisfaction, lower financial rewards, and fewer opportunities for upward mobility.

#### *Corporate response to external forces*

Mattel's initial response to external challenges was bold and unequivocal and it achieved its desired result. However, maintaining that response required that Mattel must make a long-term commitment to GMP with its conditions of complete transparency, third party external monitoring, and compliance verification. It was hoped that this approach would engender strong public support and pressure the rest of the toy industry to follow suit.

Unfortunately, this did not happen. Public and NGO campaigns against sweatshops were short-lived and could not be sustained without consumer support in the marketplace. While at the corporate level, the cost of GMP compliance, i.e., improving conditions in the factories to comply with Mattel's standards, was not materially significant when measured as a proportion of total production costs or sales prices. However, these costs were significant at the procurement level compared to the company's competitors. Consequently, Mattel's field managers felt pressured to minimize and delay compliance to contain costs. From ICCA's perspective, this widened the gap between Mattel's GMP promise and actual compliance and brought further pressure on Mattel. Under the circumstances, Mattel chose to discard its GMP compliance based on cost-benefit analysis. It did not see any material or reputational

benefit by adhering to its GMP. Instead, it opted for the industry-wide voluntary code of conduct called ICTI Care, which provided no third party, independent external monitoring. Nor did it call for public disclosure of audit findings.

#### **Notes**

<sup>1</sup> Mattel could legitimately argue that it had not abandoned its code of conduct, i.e., GMP, and continues to implement it. However, as we shall discuss in the article, Mattel terminated two of the main principals that made its code unique and different from other individual company or industry-wide codes. These were: (a) an independent third party external monitoring of Mattel's compliance with its code; and, full public disclosure of audit findings (including deficiencies found by the auditors and corrective action taken by the company). These principals were also the prime reason, which impelled Mattel to stay and of the industry-wide voluntary code called ICTI Care. At the time, Mattel discontinued its external monitoring system; it joined the toy industry's ICTI Care program. This program professes to carry out independent audits. However, it does not provide any details as to how these audits are carried out, so that one might assess the quality and independent character of these audits. Second, the findings of these audits are not publicly disclosed.

<sup>2</sup> Comments made by Robert A. Eckert, chairman and CEO, Mattel, Inc., to MIMCO members at a meeting at Mattel headquarters in El Segundo, California, on October 4, 2000.

<sup>3</sup> All audit reports cited in this article are available on Mattel and ICCA's websites: <http://www.sicca-ca.org/reports.php>.

<sup>4</sup> MDC has been an exception to this separation of responsibility and authority; Mattel has exercised full control over the entire plant regardless of the legal partnership structure.

<sup>5</sup> For the purposes of this discussion, even though the first formal audit of the MDC facility took place following its opening in 2000, its findings are reported as a part of the first round of audits in 1999.

<sup>6</sup> This situation was dramatically stated in the case of Nestle and the Infant formula boycott controversy. During the early stages of the controversy, the decentralized organization proved ineffective in responding to public pressure because the source of the problem was in one region while the source of public pressure was in another part of the world. Thus, the problems of turf, budgetary constraints, and the differing management



style and operational tactics in the two regions contributed to an exacerbation of the problem. Consequently, the top management of Nestle in Switzerland took control of the problems, and installed a separate management team in Washington, D.C. which would report directly to the Nestlé's top management and bypass the authority of the area manager in the United States as well as the managers responsible for the worldwide marketing of infant formula products. This turned out to be a most innovative and effective approach. Within 4 years, the new organization not only resolved the issues but caused a 180° turn around in Nestlé's reputation from a highly negative to a substantively positive level.

The *ad hoc* organization, however, could not be integrated into the Nestlé's existing global organization and decision-making structures. Soon after the issue was resolved, the new organization was dissolved and all authority to manage infant formula marketing reverted to the regular managers. Once in power, these managers undertook to erase all credit for resolving the issue from the new *ad hoc* organization. Instead, Nestle commissioned a journalist to write a book for general public distribution at Nestlé's expense. This book rewrote the history of the infant formula controversy as Nestlé's executives wanted the world to see. It placed all the blame of the controversy on the Nestlé's critics and projected Nestle as the hapless victim of NGOs less than ethical conduct and spreading of inaccurate and misleading information. It also largely credited the Nestlé's seasoned managers for successfully handling the issue with only a minor role assigned to the *ad hoc* organization. See Sethi (1994) and Sethi and Bhalla (1993).

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