



WORKER RIGHTS CONSORTIUM

**WORKER RIGHTS CONSORTIUM ASSESSMENT  
PT KIZONE (INDONESIA)  
FINDINGS, RECOMMENDATIONS AND STATUS**

**January 18, 2012**

## **I. Introduction**

This report outlines the findings and recommendations of the Worker Rights Consortium (WRC) concerning labor rights violations at PT Kizone, an apparel factory located in Tangerang, Indonesia. Prior to its closure, the facility employed roughly 2,800 people. The plant produced collegiate licensed apparel for the adidas Group and Nike, as well as non-collegiate apparel for Dallas Cowboys Merchandising and other brands.

### *Code of Conduct Violations*

The WRC's investigation documented violations of university codes of conduct at PT Kizone – specifically, violations of Indonesian law concerning compensation. The investigation was initiated in April 2011 after the WRC was alerted by Nike that the factory owner had fled the country and left no money to pay legally mandated severance to the workforce.

The violations at PT Kizone began on September 3, 2010, when it stopped paying mandatory terminal compensation to workers separated from employment. Between September 3 and December 31, 2010, 49 workers voluntarily left the factory's employ, but were not paid the compensation required by law and the extant collective bargaining agreement. The crisis deepened on January 5, 2011, when PT Kizone failed to provide the factory's workers with their monthly pay for December 2010. On January 31, the owner of PT Kizone, Jin Woo Kim, a South Korean national, fled Indonesia, precipitating the factory's eventual closure and leaving no money to pay severance. Green Textile, the buying agent for Nike and adidas, and the direct buyer for the Dallas Cowboys, assumed effective control of the factory's operations after the flight of the owner and kept the factory in operation for approximately nine weeks, during which time workers received their back wages. At the end of March 2011, the factory ceased operations. At the time of final closure, on April 1, 2011, the employees were owed US\$3.4 million in total, an amount representing, on average, nearly a year's base income per worker. There are 2,686 employees who are owed terminal compensation.<sup>1</sup>

To date, an amount just short of half of the terminal compensation owed to the employees has been generated. This includes \$1 million contributed (at Nike's urging) by Green Textile, a buying agent that placed orders at the factory for Nike, adidas and other customers, and \$521,000 contributed directly by Nike. The Dallas Cowboys have pledged to provide \$55,000 but, as of the date of this report, have not distributed the funds. More than 50% of the original legal severance entitlement is still owed to employees. In addition, legally mandated death benefits are owed to the families of several employees who died between September 1, 2010 and December 31, 2010.

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<sup>1</sup> This figure is according to calculations performed under the auspices of the Indonesian government.

*WRC Recommendations and the Response of University Licensees*

Under university codes of conduct, it is the duty of licensees to correct code violations, including non-compliance with domestic legal mandates. In the case of non-payment of legally mandated compensation, remediation requires that workers be paid the funds they are legally owed. This is the remedial action that the WRC has recommended.

As discussed in this report, a licensee has a variety of options to fulfill this obligation: ensuring that the workers are made whole by the factory itself or through the liquidation of the factory's assets; compelling any agent or other intermediary acting on the licensee's behalf to provide workers the required funds; or making workers whole through the use of the licensee's own resources. Whatever course of action the licensee chooses, the measure of code of conduct compliance is whether the workers are paid the compensation they are owed in full.

In this case, because PT Kizone's owner has absconded, leaving the now bankrupt company with massive debts to a range of creditors, there is no realistic prospect that the owner will pay or that the workers will be made whole through the liquidation of the factory's assets.

Therefore, if the buyers do not compel the buying agent, Green Textile, to make the workers whole, or do so using their own funds, the likely outcome is that workers will never be paid the money they legally earned.

As of the date of this report, each university-related company involved has contributed funds or pledged to do so, with the exception of adidas. Adidas has taken the position that it has no obligation to provide funds to the affected workers. Adidas has reported taking some steps that, the company argues, are appropriate under the circumstances – convening meetings of Indonesian and Korean government and industry officials, and encouraging other adidas contract suppliers in the area to consider hiring former Kizone workers – but these steps will not correct the violations of worker rights and university codes that have been committed. Even if assistance with employment opportunities is pursued effectively, in close cooperation with worker representatives, it would not do anything to pay workers the money they are legally owed. It is also highly unlikely that meetings involving government and industry officials in Indonesia and South Korea will result in any money being paid to the workers.

Adidas has justified its refusal to pay the workers on two bases: 1) that it left the factory before the violations occurred, and 2) that it has no obligation to contribute financially in cases where its contract suppliers fail to pay workers money they are legally owed.

The first justification is without any basis, as explained in detail later in this report: adidas, by its own admission, was producing at PT Kizone into late November of 2010. The violations began in September of 2010. Moreover, adidas reported PT Kizone as a supplier factory in January of 2011 – in both its mandatory collegiate disclosure and through its voluntary web-based disclosure process.

The second justification has no more weight than the first. Adidas, echoing the position it has taken in previous cases at both collegiate and non-collegiate factories, says that because it outsources production to contractors, it cannot be held financially responsible when the workers who make its clothing are robbed of the pay they have earned. However, university codes of conduct require licensees to ensure compliance by contractors, as well as directly-owned factories. University codes do not exempt contractors; if they did, there would not be much point in the codes, since the vast majority of university apparel production is outsourced.

The WRC's communications with adidas have not led to any substantive change in the company's posture in this case. We are hopeful that direct engagement by adidas' licensor universities will have an impact.

We also discuss in this report an additional challenge in addressing cases of this kind that involve multiple university buyers: whether responsibility for remediation can be apportioned among the buyers. Nike has provided funds to the workers – directly and through Green Textile – in proportion to its reported share of the factory's output. The Dallas Cowboys, more recently, have pledged to do the same. Nike's contribution has been very substantial (\$1.2 million by its accounting); the Cowboys' contribution is very small (\$55,000). Both companies, however, are taking a position with no grounding in university codes, which do not limit licensees' obligations to partial remediation of code violations. If workers are compensated in full, then licensees may apportion the cost among themselves in any manner they deem fair. However, where workers are still owed legally mandated compensation, each licensee remains in violation of university codes until that problem is fully addressed. Thus, while Nike has done far more than the other companies involved – in terms of financial contributions and transparency – we must take issue with the company's position that partial payment is adequate under applicable codes.

The contrast between Nike's response and adidas' is nonetheless very important to note. Nike disclosed the non-payment of severance, accepted responsibility under university codes, and made very substantial payments to workers in order to remedy the violations. Adidas did not disclose the violations, denied responsibility, and refuses to pay anything.

The WRC continues to recommend that all licensees take whatever steps are necessary to ensure that workers are paid all funds legally owed them. We also recommend that adidas reverse its position, accept responsibility, and contribute to the remediation process.

We will continue to monitor the situation at PT Kizone closely going forward and will report on further developments.

## II. Methodology

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

- Individual interviews with 34 PT Kizone workers.
- Meetings and communications with the Branch Leadership Board (Dewan Pimpinan Cabang) of the Serikat Pekerja Textil, Sandang dan Kulit (SP TSK-SPSI), the labor federation to which PT Kizone's factory-level union is affiliated, as well as with representatives of the plant-level union.
- Extensive communications with Nike, adidas, Dallas Cowboys Merchandising, and Green Textile.
- Review and analysis of a range of documentary evidence,<sup>2</sup> including, but not limited to:
  - Worker-by-worker calculations of severance and other terminal compensation owed to the PT Kizone workforce;
  - Agreements between Green Textile and the plant-level union at PT Kizone and between Green Textile and individual workers;
  - Filings made by PT Kizone creditors to the Central Jakarta Commercial Court and findings of the Court;
  - Findings of the government mediator appointed to the case by the Indonesian Ministry of Manpower and Transmigration, documents filed with the mediator by worker representatives, and correspondence between the mediator and the concerned parties;
  - Records of payments made to workers by Green Textile;
  - Reports and analyses of prior unpaid severance cases in Indonesia, prepared by US, European and Australian non-governmental organizations;
  - Consultation with Indonesian attorneys and worker advocates.
- Review of United States Customs data relating to the content and time-frame of shipments from PT Kizone to buyers in the United States.
- Analysis of Indonesian employment and commercial statutes as they pertain to terminal benefits for employees, supplemented by consultation with local legal experts.
- Review of media coverage of the case in the Indonesian-language press.

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<sup>2</sup> Many documents were reviewed in the original Bahasa Indonesia; translations, where necessary, were done by the WRC staff.

- The findings reached by the WRC on the basis of this evidence are outlined in section IV of this report; recommendations and the present status of remediation follow in sections V and VI.

### **III. Chronology**

As background to the presentation of the WRC's findings and recommendations, we include below a chronology of key events at PT Kizone between September of 2010 and April of 2011.

- On September 3, 2010, violations of workers' rights to legally mandated terminal compensation began at PT Kizone. On that date, the factory stopped paying mandatory compensation to employees upon separation from employment. From September 3, 2010 through the end of the calendar year, 49 employees were separated from employment, but were not paid the legally required terminal benefits due to them.<sup>3</sup> Also, during that time period, five PT Kizone employees died (of non-work related causes) and the factory failed to pay legally mandated death benefits to their families.
- On January 5, 2011, PT Kizone failed to provide employees with their monthly pay for December; this non-payment of wages affected the entire workforce. Although workers complained to factory management, most continued working and the facility remained in operation.
- On January 31, 2011, the owner of PT Kizone, Mr. Jin Woo Kim, absconded to his native South Korea, and abandoned the business. Lower management continued to operate the factory, under the guidance of Green Textile.
- On or around February 7, 2011, workers learned through informal communications with lower management of the owner's abandonment of PT Kizone. PT Kizone also failed that week to pay workers their wages for the month of January. Workers responded with public protests, leading to media coverage in Indonesia.
- On or around February 15, 2011, a contingent of workers marched to the regional office of the Indonesian labor ministry to demand that the factory pay the compensation due to them.
- At the end of March 2011, the factory ceased production. During the final weeks of operation, Green Textile paid employees their back wages for December and January

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<sup>3</sup> The workers are entitled to "separation pay," consisting of (1) a payment required under Article 61 of the plant's collective bargaining agreement and (2) payment in lieu of benefits/entitlements as per Article 162(1-2) of the 2003 Act. This was affirmed in findings issued by the regional office of the Ministry of Manpower and Transmigration of Tangerang on April 13, 2011.

out of the proceeds of completed orders – but failed to pay legally mandated terminal compensation owed to employees who had left the factory’s employ since the beginning of September 2010 and failed to make provision for payment in full of terminal compensation to the employees about to be laid off.

- Instead, on March 30, 2011, Green Textile and the plant-level union signed an unusual agreement in which the union accepted payment of only 30% of the terminal compensation legally owed to the employees about to be terminated with the closure of the factory (\$1 million) and agreed that employees would not seek the remainder from Green Textile.<sup>4</sup> The plant-level union’s agreement not to seek further compensation was opposed by the district-level leadership of the parent union, known as the Branch Leadership, or DPC. Many workers continued to seek full payment and the DPC continued to advocate for them.
- On April 1, 2011,<sup>5</sup> the factory was officially closed. The following week, Green Textile paid the \$1 million to employees, leaving \$2.4 million of legally mandated compensation unpaid.
- On April 14, 2011, the Central Jakarta Commercial Court stated that PT Kizone had been brought into bankruptcy following a filing by one of the company’s creditors. Its assets went into court-managed receivership.

#### **IV. Findings**

##### *Non-Payment of Legally Mandated Terminal Compensation*

It is the WRC’s conclusion that PT Kizone failed to pay 30.8 billion Indonesian Rupiah (Rp) (\$3.4 million) in legally mandated terminal compensation to 2,686 employees, beginning on September 3, 2010 and continuing through the date of the factory’s final closure in April of 2011. It is important to note that these facts are not in dispute: all parties agree that the severance violations occurred and that the majority of workers’ legal entitlement remains unpaid. In failing to fulfill this mandate, PT Kizone violated Indonesian law and university code of conduct provisions requiring 1) compliance by collegiate producers with applicable law in general, and 2) payment of all legally mandated benefits, specifically.<sup>6</sup>

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<sup>4</sup> Agreement between PT Green Textile and PUK TSK SPSI (Tangerang), signed on March 30, 2011.

<sup>5</sup> Communication from Green Textile May 25, 2011.

<sup>6</sup> For example, the language in the Collegiate Licensing Company’s “Special Agreement Regarding Labor Codes of Conduct,” which is the basis for the language in many university codes, states “Licensees must comply with all applicable legal requirements of the country(ies) of manufacture in conducting business related to or involving the production or sale of Licensed Articles” and “Licensees shall...provide legally mandated benefits.” The WRC Model Code Conduct, also the basis for many university codes, contains the same requirements.

Subsequent to the closure of PT Kizone, Green Textile, largely at Nike's behest, paid \$1 million to the workers in partial fulfillment of the factory's severance obligations. Nike then paid an additional \$512,000. The Dallas Cowboys have pledged to pay \$55,000. As of the date of this report, subtracting the amounts paid and pledged, the employees are still owed more than half of their legally mandated terminal compensation: \$1.8 million. As discussed below, PT Kizone's failure to pay the workers in accordance with the law has meant serious hardship for the workers and their families.

In the remainder of this section, we:

- review Indonesian law governing terminal pay,
- provide additional detail concerning the amounts owed to PT Kizone employees,
- explain the process through which the amount due to each person was calculated,
- review the circumstances under which Green Textile paid \$1 million to the workers, and
- discuss the bankruptcy proceedings and their implications for workers.

#### *Indonesian Law Concerning Terminal Compensation*

The Law on Manpower (Act No. 13 of 2003, henceforth the 2003 Act) establishes that workers are entitled to full standard terminal compensation when their employer has gone bankrupt, as occurred in the case of PT Kizone.<sup>7</sup> Under the statute, compensation includes the following, for each worker:

- "Severance pay" at a rate of one month's base wages for each year of service, up to a maximum of nine months' pay.<sup>8</sup>
- "Reward pay for services rendered," consisting of an additional month's pay for every three years of service, up to a maximum of ten months' pay.<sup>9</sup>
- "Compensation pay," including<sup>10</sup>:
  - Compensation for unused annual leave that has not expired;

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<sup>7</sup> See 2003 Act, Art. 165. Such standard severance is also required in the case of economic layoffs, as well as where the facility closes down following two consecutive years of lost profits or due to force majeure, Art. 164(1), or where the ownership of the business changes and workers do not wish to remain employed, Art. 163. Additional severance is required where a business is shut down per the owner's prerogative for rationalization. Art. 164(3).

<sup>8</sup> 2003 Act, Art. 156(1).

<sup>9</sup> *Id.*, Art. 156(2).

<sup>10</sup> *Id.*, Art. 156(3).

- Costs or expenses for transporting the worker and their family back to the place of hire;
- Compensation for allowances for housing, medication, and health care, at a rate of 15% of the severance pay and reward pay, for those workers who are eligible for such compensation;
- Any other compensation that is required by an employment contract or collective agreement.

Additionally, workers who resigned voluntarily from PT Kizone, prior to its closure and bankruptcy, are entitled to terminal compensation under Indonesian law and the factory's collective bargaining agreement.<sup>11</sup> Workers are entitled to this benefit once they have served at least three years. The compensation formula ranges from two months' pay for workers who have worked more than three years to seven months' pay for workers who have worked more than seventeen years.

Finally, Indonesian law requires payment of death benefits to the families of deceased workers, which include severance accrued by a worker up to the time of his or her death.<sup>12</sup>

#### *Amount Legally Owed to PT Kizone Workers*

Calculations for the payment of terminal benefits to PT Kizone workers were carried out in accordance with these legal provisions. In Indonesia, terminal benefits are calculated for each worker through a tripartite process involving worker representatives, company representatives, and the regional office of the Ministry of Manpower and Transmigration (the Ministry of Manpower is the official name of Indonesia's labor ministry). In this case, because of the owner's abandonment of the business, the employer did not participate; calculations were carried out by the labor ministry in Tangerang and worker representatives (specifically the DPC) in May 2011. Management was invited to participate in the process, but failed to appear.

The process identified 2,686 employees who are legally entitled, in the aggregate, to 30.8 billion Rp in terminal compensation. At the Interbank exchange rate<sup>13</sup> prevailing on January 13, 2012, the equivalent in US dollars is: \$3.4 million. This total includes 26.1 billion Rp (\$2.9 million) in severance and reward pay; 3.9 billion Rp (\$431,358) in compensation pay; and 96.6 million Rp (US \$10,637) in death benefits for the families of five employees. Of the overall entitlement, 256 million Rp (\$28,200) is due to 49 employees who left the factory's employ between September 3, 2010 and December 31,

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<sup>11</sup> Collective Bargaining Agreement between PT Kizone International and PUK SP TSK SPSI (2008-2010), Clause 61.

<sup>12</sup> Article 166 of Act No. 13 of 2003 on Manpower.

<sup>13</sup> All currency conversions in this report use the January 13, 2012 rate, which was 9,082.96 Rupiah to the US Dollar.

2010; 34 of these employees left PT Kizone, and were illegally denied their terminal pay, prior to the date on which adidas says it completed its most recent production run.

The following chart provides additional detail on the disposition of the legal severance entitlement at PT Kizone.

<b>PT Kizone: Compensation Legally Owed to Employees</b>		
	<b>Amount in Indonesian Rupiah</b>	<b>Amount in US Dollars</b>
Severance and Reward Pay Legally Owed	26,120,052,816	2,875,720
Compensation Pay Legally Owed	3,918,007,922	431,358
Death Benefits Legally Owed	96,615,144	10,637
Resignation Benefits Legally Owed	611,107,767	67,281
<b>Total Legally Owed Prior to Buyer Payments</b>	<b>30,745,783,649</b>	<b>3,384,996</b>
Funds Paid by Nike and Green Textile	13,815,182,160	1,521,000
Funds Pledged by Dallas Cowboys	499,562,800	55,000
<b>Amount Still Legally Owed</b>	<b>16,431,038,689</b>	<b>1,808,996</b>

*Partial Payment by Green Textile*

On March 30, 2011, Green Textile, which was effectively operating the factory, signed an unusual agreement with PT Kizone’s plant-level union. Under the agreement, Green Textile agreed to contribute a total of \$1 million to the PT Kizone workforce, an amount representing approximately 30% of the debt owed to the employees, in exchange for a commitment that employees would not seek any additional funds from Green Textile. The funds were distributed to employees a week after the closure.

While it is, of course, positive that workers received the \$1 million paid by Green Textile, it was not appropriate for Green Textile to ask for a commitment from the union not to seek the remainder. It was also not appropriate for Nike, adidas and the Dallas Cowboys to suggest, as they originally did, that this agreement constituted a legitimate resolution of the case, a position they fortunately later abandoned in response to the WRC’s exposure of its illegitimacy. University codes of conduct require licensees to ensure that

their factories pay workers in accordance with the law. An agreement whereby workers accept less than legal minimum compensation violates this standard. The same would be true if a union were to sign an agreement with a factory saying it is permissible to not pay workers for overtime, or to never give them a day off, or to pay less than the legal minimum wage. Thus, as far as university codes are concerned, the union's commitment not to seek the remainder of the funds legally owed to workers carries no force. In addition to the union's collective commitment that workers would refrain from seeking full compensation, Green Textile required each individual worker, as a condition of receiving payment, to sign a document stating that he or she would not seek any further compensation from Green Textile. These individual agreements were illegitimate for the same reason outlined above.

It is also important to note that serious questions have been raised about the legitimacy and the motives of the factory-level union officials who signed this agreement and that most workers have now formally asked the DPC (the district-level union) to represent their interests. Worker testimony indicates that the deal to accept 30 cents on the dollar was made before many workers had even authorized the union officials to negotiate on their behalf. The DPC denounced the agreement as morally illegitimate and challenged the propriety of the factory-level officials' actions.<sup>14</sup>

While the history reviewed here is relevant for context, the issue of the collective and individual worker commitments not to seek further compensation is now moot. All of the licensees now accept that workers are still legally owed their full severance. The PT Kizone workers continue to seek full payment and the DPC continues to advocate on their behalf – and neither Green Textile, nor any other party, has attempted to constrain them from doing so.

Additionally, under the agreement, if Green Textile were to fail in its efforts to buy PT Kizone, and if the ultimate buyer were then to agree to pay workers some of the severance they are owed, this money would go not to the workers, but to Green Textile – until Green Textile is paid back for its \$1 million. Fortunately, it is highly unlikely that Green Textile will press this unreasonable claim, and it is furthermore unlikely that such an effort would be successful.

The motivation of Green Textile in paying the \$1 million is not entirely clear. The biggest factor underlying Green Textile's decision to pay, we believe, was encouragement from Nike, which, in the wake of university concern in 2010 over non-payment of severance to the workers at the Hugger and Vision Tex factories in Honduras, appears to be taking a more pro-active approach to addressing such cases. Also, at the time of the payment, Green Textile had told interested parties that it was seeking to buy PT Kizone and re-open the factory at a later date. It may have made the payment, and secured its deal with

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<sup>14</sup> An additional example of the modus operandi of the factory-level union is that it subsequently circulated a letter (dated May 27, 2011) threatening that workers who formally requested that the DPC represent them would have to return the funds provided by Green Textile or be subject to legal action.

the plant-level union, partly in order to ameliorate the anger of the workforce (in the hope of attracting skilled workers back to the factory if it re-opened), while also relieving itself, as the prospective owner, of the obligation to pay the majority of the severance legally due. Whatever the case, and notwithstanding the illegitimate aspects of the agreement, the \$1 million was paid and has made the situation for workers and their families considerably better than it would otherwise have been.

### *Bankruptcy Proceedings*

The processing of PT Kizone's bankruptcy, including the liquidation of assets, has proceeded slowly and, despite a recent sale of assets, is unlikely to yield substantial funds for workers.

PT Kizone was brought into court-managed receivership in April 2011. On December 16, 2011, a buyer (a Taiwanese company with no previous involvement in the case) acquired the bulk of PT Kizone's assets. Creditors are now waiting to hear the decision of a court-appointed receiver regarding how the proceeds from this sale will be distributed. Unfortunately, as outlined below, the total amount raised from the liquidation of the company's assets is grossly exceeded by the total claims of the company's various creditors, including its workers. Most significantly, the proceeds are less than the amount owed to secured creditors, whose claims are, unfortunately, regularly granted precedence in Indonesia over those of workers.

### Workers' rights under Indonesian bankruptcy law

While the Law on Manpower (Act No. 13 of 2003) grants some level of priority to workers when their employers enter bankruptcy,<sup>15</sup> other statutory provisions, specifically the country's civil code and its Law on Bankruptcy and Suspension of Obligation for Payment of Debts (Act No. 37 of 2004), establish that certain other categories of creditors are privileged above workers. The Book of Civil Code, the basic civil law established by the Dutch colonial government in 1847 which was retained following Indonesia's independence, states that liens and mortgages shall take precedence over any other debts, including those granted a special status, unless another law specifically states to the contrary (Article 1134). The 2004 Law on Bankruptcy reaffirms this principle and specifically grants super-priority to any creditors "whose claims are secured by lien, fiduciary security, security right, mortgage, or other collateral rights on property, or those having priority rights on an asset within the bankruptcy estate" (Article 138).<sup>16</sup> (Such creditors, commonly referred to as "secured creditors" in the US context, are known in Indonesian legal parlance as "separatist creditors.") In addition, Indonesian tax law also

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<sup>15</sup> Article 95(4): "if a company is declared bankrupt or liquidated... workers' wages and other entitlements shall be prioritized."

<sup>16</sup> This category of creditors is known in Indonesian as "separatist creditors." This is similar to the U.S. concept of "secured creditors."

grants priority to debts to government entities, such as unpaid taxes and utility bills,<sup>17</sup> over the claims of other creditors, including workers.

Indonesian Courts typically have held that the law should be interpreted to prioritize secured creditors above workers. In 2008, Indonesia's Constitutional Court rejected the argument of the former employees of the firm PT Sindoll-Pratama that the bankruptcy law's prioritization of the claims of secured creditors over those of workers violates the Indonesian Constitution.<sup>18</sup> The Constitutional Court did not contest the petitioners' statements that workers were disadvantaged in the bankruptcy system, but rejected their claim that this contradicted the Constitution. The petitioners' attorney, Dr. A. Muhammad Asrun, summarized the experience of 1,045 PT Sindoll-Pratama workers in the bankruptcy process as follows: "all of the company's machines, the building, the land, and even the private assets of the commissioner and primary director... was auctioned and sold by Bank Negara Indonesia in May 2007 and August 2007, without one single rupiah being received by the workers in recognition of their right to proper wages and compensation."<sup>19</sup>

The Constitutional Court confirmed in its decision that, "workers, as preferred creditors, have a lower status than separatist creditors, so if the assets of the employer are claimed as collateral and seized by the separatist creditors, this may result in the workers not receiving anything."<sup>20</sup> The Court concluded that workers' constitutional rights were not violated under this interpretation of the statutes. The Court did suggest that "various social policies" should be used to improve workers' position and that there should be better "synchronization and harmonization of [the relevant] laws," but opposed any action that would "disturb the interest of separatist creditors." The Court's rationale included a concern that any infringement on the right of "separatist creditors" to be prioritized would "reduce... incentive and motivation for investors to make investments," thus inhibiting job creation. No improved social policies or "synchronization and harmonization of laws" as recommended by the Court have taken place.<sup>21</sup>

The WRC has consulted with a number of lawyers and workers' rights advocates in Indonesia regarding the outcome of similar cases in the past. They consistently reported that workers are rarely made whole through the bankruptcy process for the compensation

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<sup>17</sup> Article 21 of Law Number 16 of 2000 regarding General Tax Provisions and Procedures, as most recently amended by Law Number 28 of 2007 regarding the Third Amendment to Law Number 6 of 1983 regarding General Tax Provisions and Procedures.

<sup>18</sup> Constitutional Court Decision Number 18/PUU-VI/2008

<sup>19</sup> Workers were ultimately able to win partial payment through the latitude granted all receivers. However, the court did not contest the fact that the initial outcome clearly fulfilled the letter of the law. Session minutes for 26 August 2008 in Case 18/PUU-VI/2008 and "Test of the Bankruptcy Laws: Workers Want to be Equal with Separatist Creditors." Constitutional Court blog 16 July 2008. <http://www.mahkamahkonstitusi.go.id/index.php?page=website.Berita.Berita&id=2476>

<sup>20</sup> Constitutional Court Decision Number 18/PUU-VI/2008

<sup>21</sup> Constitutional Court Decision Number 18/PUU-VI/2008

they are legally-owed. Court-appointed receivers have significant latitude in deciding the distribution of funds. The final division of funds, however, is based on negotiation between the creditors and the receiver, and workers generally receive only a small percentage of the funds they are owed, if any. One employment lawyer who has dealt with ten bankruptcy cases stated, in a 2010 forum on the subject, that factory workers' only hope to be made whole is to physically take control of the assets of the factory immediately upon its closure. Otherwise, he said, the court proceedings rarely result in the workers receiving a significant share of the funds they are owed.

One recent example of such an outcome is the case of PT Great River International, which operated three factories in the greater Jakarta area employing approximately 9,000 workers. According to interviews with an attorney representing the workers, the Indonesian Industrial Relations Court (PHI) found in 2007 that the workers were due significant severance and back wages. Nearly five years later, however, this compensation remains unpaid. In 2010, the company formally entered bankruptcy. Claims by workers and other creditors against the assets of each of the three factories have been adjudicated separately by the bankruptcy court. At two of the factories, in Bogor and Purwakarta, the bankruptcy process has been completed and workers have received no compensation at all – the entirety of the funds raised through the sale of factory assets were distributed to the secured creditors. The workers are appealing the distribution but have little hope of success. At the third factory, in Bekasi, the bankruptcy proceedings continue. The workers' attorney states that if they are extremely lucky, the workers at this third factory may receive a percentage of what they are due.

#### Kizone bankruptcy proceedings

PT Kizone was declared bankrupt on April 14 after a creditor informed the court that PT Kizone had failed to meet its financial obligations to that lender. The interests of most of the PT Kizone employees are represented in the bankruptcy proceeding by the DPC. On May 20, 2011, the DPC submitted a calculation of PT Kizone's obligations to employees to the Central Jakarta Commercial Court. The total currently owed to employees is \$1.8 million.<sup>22</sup>

In accordance with Indonesian law, the court initially sought a buyer who would purchase PT Kizone as a single entity. When no such buyer was found, the court-appointed receiver conducted an auction in two phases. In the initial phase, vehicles and an apartment owned by the company were sold for 7.5 billion Rp (\$83,013). In the second phase, on December 16, 2011, the factory itself and related physical assets were purchased in public sale for 25.5 billion Rp (\$2.8 million) by an Indonesian citizen,

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<sup>22</sup> The claim made by the workers to the court totals 43.7 billion Rp (\$4.8 million), which is the total amount that PT Kizone failed to pay workers, including unpaid wages. However, this number does not take into account the payments that have been made by other sources, including Green Textile and Nike. While the receiver may choose to rely on the higher number, it is highly likely that, when it comes to the distribution of funds, he will rely on the sum the workers are currently owed, 16.4 billion Rp (\$1.8 million).

Hartono Sukir, who was representing a Taiwanese firm. The total amount of money generated by the sale is thus 26.2 billion Rp (\$2.9 million).

The \$2.9 million dollars available to pay the company's creditors represents less than 14% of total outstanding claims. On June 15, 2011, the Commercial Court stated that it had received claims from creditors totaling 183.9 billion Rp (\$20.3 million).<sup>23</sup>

Most importantly, two of the company's creditors, a bank and a venture capital firm, are classified as "separatist" creditors, the category that, as noted, is given super-priority under the bankruptcy law. These two creditors' claims alone total 28.7 billion Rp (\$3.2 million), more than the amount raised by the auction. If the secured creditors are given first priority, as is likely, the workers will receive nothing.

In addition, the government's Indonesian Customs & Excise Office is owed 3.0 billion Rp (\$335,315).

The receiver has yet to announce how these proceeds will be distributed among the creditors, or to announce a timeline by which this decision will be made. The receiver has some latitude in distributing the proceeds of the sale and there are several possible scenarios:

- The receiver may prioritize the secured creditors (as in the PT Sindoll-Pratama case), using all of the funds to partially repay those two entities. In this scenario, the workers will receive no funds from the bankruptcy process. This is the most likely outcome.
- The receiver may prioritize the secured creditors, but may set aside some modest sum to partially repay the workers and the debt owed to the government. The receiver can determine what percentage is appropriate based on his own judgment. If, for example, the receiver allocated 20% of the funds to divide between the government and the workers, Kizone employees would receive 4.4 billion Rp (\$487,695) – roughly 27% of what workers are still owed.
- The best case scenario for the workers, but the least likely, is that the receiver will choose to treat the claims of the workers and the government as co-equal with those of the separatist creditors. In this case, if the funds were divided among these four classes of creditors proportionally to the size of each class' claim, PT Kizone employees would receive 9.0 billion Rp (US (\$986,340) – still only slightly more than half the amount they are owed.

Given that Kizone's liabilities outstrip the amount of money generated by the sale of its assets, and given that the claims of the secured creditors are greater than the funds

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<sup>23</sup> "List of Recognized Claims." Issued by Receiver Anggi Putra Kusuma, S.H. on June 15, 2011.

available, there is no realistic chance of workers being made whole through the bankruptcy process.

The chair of the DPC has advised the WRC that the union has minimal expectations of the process. In a recent communication to the WRC, he stated: “Considering our experience with other bankruptcy processes in Indonesia, as well as the fact that PT Kizone’s debt is greater than the value of the assets, we are sure that workers will receive a very small share of the auction proceeds, and certainly not the amount due to them under labor law.”

Further action by university licensees is therefore essential if the violations at PT Kizone are to be fully corrected and workers are to be made whole.

## **V. WRC Recommendations**

University codes of conduct require compliance with applicable law generally<sup>24</sup> – and payment of legally required benefits in particular.<sup>25</sup> It is the obligation of licensees to ensure compliance. In cases where factories fail to pay workers compensation to which they are legally entitled, it is the responsibility of licensees sourcing from the factory to take whatever steps are necessary to ensure that workers are paid in full.

In the case of PT Kizone, beginning in April 2011, the WRC recommended that the brands involved – Nike, adidas, and the Dallas Cowboys – take whatever steps are necessary to ensure that the PT Kizone workers are paid the outstanding compensation legally due to them. As the WRC has conveyed, licensees may accomplish this result through whatever means they prefer. What is crucial from a code of conduct compliance standpoint is that workers are fully paid.

## **VI. Licensee/ Brand Responses**

This section outlines the response of adidas, Nike, and the Dallas Cowboys to the WRC’s recommendations and certain additional findings relative to those responses. Before reviewing the posture of each company in turn, we set out in the following table a summary of actions taken to date by the companies involved and the progress thus far achieved toward remediation of the violations:

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<sup>24</sup> See, e.g., Collegiate Licensing Company, *Code of Conduct*, Schedule I, Section II(A).

<sup>25</sup> See, e.g., *id.*, Section II(B)(1).

<b>Summary of Buyer Remediation Efforts (US Dollars)</b>	
Total Amount Originally Owed	3,384,996
Contributions Distributed or Pledged	
<b>Green Textile/Nike</b>	<b>1,000,000</b>
<b>Nike</b>	<b>521,000</b>
<b>Dallas Cowboys</b>	<b>55,000</b>
<b>Adidas</b>	<b>0</b>
Total Contributed or Pledged	1,576,000
Percentage Paid to Date	46.56%
Total Owed	1,808,996

The sections that follow detail the specific responses of each brand.

#### *Response of adidas Group*

In contrast to Nike, adidas has made no financial contribution to remediate the violations committed at PT Kizone and insists that it will not do so. Adidas justifies its response on two bases: 1) that PT Kizone was not an adidas supplier when the violations began, and 2) that even if PT Kizone had been an adidas supplier, adidas has no obligation under university codes of conduct to pay money to workers when its chosen contractors fail to pay then in accordance with the law. Neither claim is valid; both are addressed below.

#### Adidas' claim that it exited PT Kizone prior to violations occurring

The following facts are not in dispute:

- The labor rights violations at PT Kizone related to terminal compensation began on September 3, 2010, when the company stopped paying terminal compensation to workers. Thirty-two workers were denied legally mandated compensation upon separation from employment between September 3, 2010 and November 1, 2010. The factory also failed to pay death benefits to the families of several workers who died during this period. On January 5, PT Kizone stopped paying workers altogether. On January 31, the owner fled the country.
- Adidas was producing at PT Kizone when the violations began in September and continued to produce at PT Kizone at least through November 20, 2010.<sup>26</sup>

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<sup>26</sup> Adidas' first public admission that it had production in the factory until November 20, 2010 appears in a statement posted on its website on December 13, 2011. The statement is accessible at: [http://www.adidasgroup.com/en/sustainability/statements/2011/Playfair\\_allegations\\_about\\_closure\\_PT\\_Kizone\\_Indonesia\\_Dec\\_2011.aspx](http://www.adidasgroup.com/en/sustainability/statements/2011/Playfair_allegations_about_closure_PT_Kizone_Indonesia_Dec_2011.aspx)

- In January 2011, adidas reported on its website that PT Kizone was still an active supplier factory. Adidas also reported to universities that same month, and again in April 2011, that PT Kizone was still a producer of university logo merchandise.

As these facts demonstrate, adidas' claim that it was out of the factory before the violations began is false. By any conceivable definition, PT Kizone was an adidas supplier factory when it committed numerous violations of Indonesian law and university codes of conduct. Adidas is therefore obligated to ensure that the violations are remedied.

Moreover, adidas, and the other buyers, should have taken action to address the violations in late 2010 and should have recognized that the factory was in financial crisis and tried to work with the factory to avoid a deeper crisis. They did not. Adidas has pledged to adhere to the guidelines concerning lay-offs and factory closures developed by the MFA Forum, a multi-stakeholder initiative in which adidas participated. These guidelines state that buyers should "monitor supplier adherence to regular and timely payment of wages and legally required benefits...[and] oversee, on an on-going basis, that sufficient resources are available to meet all employee liabilities in the event of downsizing or closure."<sup>27</sup> Adidas says it was monitoring PT Kizone's labor practices throughout the time it was in the factory, stating in a communication to universities dated November 26, 2011:<sup>28</sup> "While the commercial relationship was open, we monitored the PT Kizone workplace to ensure that it adhered to the standards and practices required..." However, since adidas took no action to correct the violations committed in the fall of 2010, while its goods were on PT Kizone's production lines, and took no action at any time to address the factory's increasingly evident financial crisis, we must conclude that adidas did not fulfill its obligation to monitor compliance and did not "oversee, on an on-going basis, that sufficient resources are available to meet all employee liabilities in the event of downsizing or closure." This poor monitoring performance in the months prior to adidas' reported departure from the factory amplifies the company's obligation to contribute meaningfully to the remediation process.

It must be noted that the effort to undo the harm done to the workers of PT Kizone has been complicated by adidas' unwillingness to acknowledge responsibility and by misleading information that adidas has circulated concerning its relationship with the factory. In letters, messages, and statements, adidas has repeatedly summarized its relationship with PT Kizone in the manner reflected in the following statement from its November 26 communication: "We cannot ourselves assume, or accept, the liability for the severance owed by the owner of PT Kizone, a factory that closed 10 months after our commercial relationship was terminated." In the same letter, adidas states: "The relationship [with PT Kizone] ended in June 2010 and the factory closed almost one year later." To generate this claimed "10 month" gap, adidas employs two rhetorical sleights of hand: First, adidas cites June 2010 as the date when its "commercial relationship" with

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<sup>27</sup> See: [http://www.fairlabor.org/fla/pub/SyncImg/mfa\\_forum\\_guidelines.pdf](http://www.fairlabor.org/fla/pub/SyncImg/mfa_forum_guidelines.pdf)

<sup>28</sup> Letter from adidas to unspecified list of universities, titled "SEA Response to PT Kizone to WRC," November 2, 2011.

PT Kizone ended, even though adidas itself admits that Kizone workers were still making goods for adidas five months later, in late November of 2010. Second, adidas cites the factory's final closure date as if it were the relevant benchmark. Since adidas' argument is that it is not responsible for the violations because it left the factory before they happened, the relevant date is obviously the date the violations began. The date of the factory's final closure, months later, is beside the point. Moreover, whether or not adidas was aware of the violations that were committed from September to November of 2010, the company is unquestionably aware that the owner fled in January 2011, since it has commented on this event in its own communications. Since adidas acknowledges that it produced at Kizone in November, and acknowledges that the owner fled in January, two months later, we don't understand how the company could, in good conscience, have ever suggested to its university partners that its dealings with PT Kizone ended "almost one year" before problems arose.

After learning that the violations began in September of 2010, the WRC wrote to adidas, sharing this information and asking if the company is now ready to acknowledge that it has a responsibility to address code violations at the factory. Adidas responded on January 18, 2012, stating: "We are still waiting for our field team in Indonesia to validate the information which you have shared." Nonetheless, adidas states that it has no intention of revising its stance, adding: "Our position regarding payment of severance to workers in lieu of unmet obligations of the owner of PT Kizone has not changed."<sup>29</sup>

Adidas' claim that it has no obligation to contribute financially to workers in order to remedy violations of university codes and wage and benefit laws

It is adidas' position that it will not pay money to workers in any case involving non-payment of legally mandated terminal compensation – whether or not it was sourcing from the factory when the violations began. In a message to the University of Wisconsin-Madison, Gregg Nebel of adidas stated the following in reference to the plight of the PT Kizone workers: "We are following existing adidas Group policies and approaches: we will not make any cash payments to workers in lieu of severance owed."<sup>30</sup>

While a refusal to contribute financially when its contractors fails to pay workers may well be adidas' corporate policy, it is university codes of conduct, not adidas' policies, which govern the company's obligations at factory's producing university logo goods.

As noted above, university codes require compliance with applicable law in general and payment of legally mandated benefits specifically. The most commonly used code of conduct language states: "Licensees must comply with all applicable legal requirements of the country(ies) of manufacture in conducting business related to or involving the

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<sup>29</sup> Email sent by Bill Anderson, adidas, to Scott Nova, WRC, January 18, 2012

<sup>30</sup> Email sent by Gregg Nebel, adidas to Vince Sweeney, University of Wisconsin-Madison, September 30, 2011.

production or sale of Licensed Articles.”<sup>31</sup> It is important to bear in mind that university codes make no distinction between factories owned by the licensee and factories working under contract. Licensees are responsible for the labor practices of their contractors as well as for practices at facilities they own. The reason for this is to ensure that licensees cannot avoid responsibility for adhering to university standards merely by subcontracting their production. Indeed, in setting forth licensees’ obligations, the most commonly used code language defines “licensee” itself to “encompass all of [the] Licensee’s contractors, subcontractors or manufacturers which produce, assemble or package finished Licensed Articles....”<sup>32</sup> Numerous codes include additional language making clear licensees’ responsibility for ensuring compliance by contractors and subcontractors. The University of Notre Dame Code, for example, requires that each licensee “ensure its compliance with this Code of Conduct and...verify that its business partners, subcontractors and others involved in the production or manufacture of products ... are in compliance with this Code of Conduct.”<sup>33</sup> The University of California Code states: “University licensees and their contractors must operate workplaces, and ensure that their contractors operate workplaces, that adhere to [the Code’s] minimum standards and practice.”<sup>34</sup> As has been recognized across the university community since codes were first adopted, the obligation to ensure compliance carries with it the obligation to correct non-compliance.

While the exact language varies among different university codes, these essential elements are, to our knowledge, universal: that licensees must comply with applicable laws, including those covering wages and benefits, and that licensees’ obligations extend to ensuring compliance with these laws by their contract factories.

In some circumstances, adidas acknowledges these obligations and acts in accordance with them; however, in cases where money is owed to workers, adidas takes a different posture. We do not see any support for this position in the language of university codes. In imposing on licensees the obligation to ensure compliance, and therefore to remedy non-compliance, the codes make no distinction between severance violations and other categories of violations. They make no distinction between violations involving cash compensation in general and those that do not. They make no distinction between violations that can be remedied at little or no financial cost and those, like the violations at PT Kizone, where a remedy requires that someone pay. We understand why adidas wants to distinguish between violations that it can correct at no cost to itself and violations where remediation may carry a price tag, but university codes of conduct do not embrace this dichotomy.

It is also important to bear in mind the role of Green Textile, adidas’ buying agent, which placed orders at PT Kizone on adidas’ behalf and which was the factory’s primary source of business. From a code of conduct standpoint, adidas is also responsible for ensuring

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<sup>31</sup> See, e.g., Collegiate Licensing Company, *Code of Conduct*, Schedule I, Section II(A).

<sup>32</sup> Id., Section I.

<sup>33</sup> University of Notre Dame Licensing Code of Conduct, Section IV.

<sup>34</sup> University of California Code of Conduct for Trademark Licensees, Section IV.

Green Textile's compliance and for ensuring that Green remedies any violations committed by its suppliers making university products. Green, which was responsible, either as an agent or direct buyer, for the majority of all orders placed at the PT Kizone, has not fully remedied the violations committed by the factory. It did pay a substantial amount to the workers (though there is no indication that adidas played a significant role in Green's decision), but left millions in severance unpaid. Since adidas has an ongoing (and, we believe, extensive) relationship with Green Textile, it has significant influence over the company. One option readily available to adidas is to press Green to pay the remaining amount owed to the workers. Adidas could also choose to ask another company, SAE-A, which adidas says it used as a buying agent at PT Kizone, to contribute financially toward a just resolution.

Whatever means adidas uses, it is obligated to remedy the violations at PT Kizone by ensuring that workers receive all of the funds they are legally owed. Adidas' claim that it is not required to do so under university codes has no substantive basis.

It is important to note that the interpretation of university codes outlined here represents the considered assessment of the WRC and it is the guidance we are providing to universities. We recognize that it is not the WRC's role to decide for any given university how it will interpret the labor rights language in its licensing agreements and how it will respond to any breach. Our responsibility is to reach findings and recommendations based on the evidence and on our understanding of the letter and intent of the applicable codes and to advise our university affiliates accordingly.

It is also important to consider adidas' position that it "will not make any cash payments to workers," in the context of the very different position taken by its primary competitor, Nike. Nike has made substantial cash payments to workers in this case, as discussed in greater detail below. Nike has also pledged to pay \$500,000 to workers in a contemporaneous case in Indonesia, at PT Dong One, where, as at PT Kizone, the owner fled without making provision for severance (adidas also sourced from PT Dong One). And, as is well known to WRC affiliate universities, Nike also made very substantial direct payments to workers at two factories in Honduras in 2010, Hugger and Vision Tex, to remediate severance violations at those facilities. Adidas has not explained why it is unwilling to take the same steps as Nike to remedy labor rights violations at collegiate factories.

#### Adidas' claim that it is undertaking meaningful remedial actions

Though it continues to insist that it has no obligation to do so, adidas has reported taking two steps to assist the workers of PT Kizone. Neither of these approaches is adequate to remedy the violations in question.

First, adidas says it is aiding workers with job placement at other factories in the region. Even if such a program were pursued effectively, which would require strong cooperation with legitimate worker representatives, it would not do anything to pay workers the money they are legally owed. In this case, the DPC has reported to the WRC that it has

never been contacted by adidas about this program and that few workers have benefited. We presume some workers will gain employment through this process; the vast majority, however, will not – absent a much more robust program and a concrete commitment from adidas to ensure jobs for specific numbers of workers. More importantly from a code of conduct standpoint, re-employment does not address the issue of the severance workers are legally owed.

Second, adidas says it has convened meetings involving government and industry officials from Indonesia and South Korea (the home country of PT Kizone's owner) to discuss the case and the broader problem of unpaid severance. It is highly unlikely that these meetings will lead to any money being paid to the workers of PT Kizone and they are therefore not a remedy to the code violations.

The history of the case of Hermosa Manufacturing, a collegiate factory in El Salvador, provides an indication of the likelihood that the measures adidas has described will restore workers' rights at PT Kizone. The Hermosa factory, a longtime adidas supplier, closed in May 2005, without paying 260 workers roughly \$825,000 in legally required terminal compensation.<sup>35</sup> As in the present case, the owner had abandoned the factory, and there was no realistic prospect of covering the debts owed to workers through liquidation of the plant's assets. Contributions by the other companies that profited from the workers' labor were therefore necessary if workers were to be made whole (and meaningful action would have come at a relatively small cost to adidas since, at the time universities became engaged, only a minority of the ex-Hermosa workforce was still in communication with worker representatives and actively seeking the compensation due them). As in the present case, adidas refused to contribute funds to help remedy the violations and instead insisted – for a period of years, and in the face of sustained stakeholder criticism – that it was providing meaningful assistance to the Hermosa workers by engaging with the Salvadoran government concerning the severance issue, by encouraging its other suppliers in El Salvador to provide the workers with jobs, and by providing job training. It must be noted that adidas had a special obligation to assist the workers in finding employment because a nearby adidas supplier, Chi Fung, was systematically blacklisting the Hermosa workers.<sup>36</sup> Nevertheless, despite adidas' frequent assurances that it was doing all that it could do – that it had coordinated with Chi Fung to open employment opportunities to workers and that it was meeting with government and industry officials about the severance issue – not a single Hermosa worker among the group in question was ultimately able to obtain employment at Chi Fung, or any other adidas supplier, and none of the workers ever received the compensation owed to them. The approach adidas is taking in the case of PT Kizone mirrors closely the approach it took at Hermosa.

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<sup>35</sup> See, e.g., WRC Update on Hermosa/Chi Fung (October 10, 2006).

<sup>36</sup> See WRC Update on Hermosa/Chi Fung (January 5, 2007).

### *Response of Nike*

The response of Nike to the PT Kizone case, though it does not satisfy Nike's obligation to achieve full remediation, has been the most constructive of the brands involved.

Nike brought the closure to the attention of the WRC and facilitated initial conversations with Green Textile in order to aid the WRC in developing a full picture of the situation on the ground. Nike's transparency with respect to the case, which has continued, has contributed to the progress that has been achieved.

Nike initially held that the agreement between Green Textile and the factory-level union, paying workers 30 cents on the dollar, obviated the need for further remediation. As discussed earlier in this report, this was not a reasonable position from a code of conduct standpoint. After the WRC exposed the illegitimacy of the agreement, Nike moved relatively quickly to recognize that further action was required.

In July 2011, following substantial discussions with the WRC, Nike announced that, along with its "supply chain partners," it would provide PT Kizone employees with \$521,000 dollars in financial assistance. Nike also informed the WRC that it considered \$650,000 of the \$1 million paid by Green Textile to be a *de facto* contribution from Nike, since, according to Nike, 65% of the orders placed at the factory by Green were for Nike. Nike announced the contribution in light of its assessment that there was not a realistic prospect that auctioning of the plant's assets would result in full payment to the workforce. It is Nike's position that the \$1,171,000 it takes credit for paying, which is 35.5% of the total owed to employees, fulfills its obligation to the workers because Nike was responsible for 35.5% of the factory's sales in its final year of operations.<sup>37</sup>

The funds contributed by Green Textile, largely at Nike's behest, and by Nike directly, have been of great benefit to workers – without these contributions they would have received nothing. Nike's actions have thus been a meaningful contribution toward the remediation of the violations at PT Kizone.

However, the WRC cannot credit Nike's position that partial payment fully satisfies its code of conduct obligations. On its face, a brand paying in proportion to its share of a factory's business may seem reasonable. However, it is important to bear in mind that the idea of partial responsibility for correcting violations is not a principle that has ever been accepted in the context of university labor codes. For example, in a case where a factory had illegally fired ten workers, we would not accept a licensee's claim that because it represented 40% of the factory's sales, it was only responsible for securing the

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<sup>37</sup> Based on the 35.5% figure, Nike calculated that its "share" of the obligation comprised \$1.17 million. Nike further calculated that a portion of Green Textile's contribution proportional to the percentage of Green Textile's production at Kizone that was for Nike should count towards its "share." This left Nike to pay, or engage its supply chain partners in paying, the additional \$521,000 pledged in July 2011 and delivered in August.

reinstatement of four of the ten workers, or for reducing toxins in drinking water by only 40% of the amount needed to make it potable for workers.

Indeed, under university labor codes, licensees are responsible for fully correcting code violations, whether they are 2% of a factory's business or 92%. If licensees choose to produce in a given factory, they are taking responsibility for making sure that the factory complies with universities' labor standards.

Once workers are compensated in full, then the buyers may divide the cost among themselves in any manner they deem equitable. However, when large sums are still owed to workers, all buyers remain responsible for correcting the violations of law and university codes.

Also, as a practical matter, given that in many university factories the collegiate buyer represents a very small percentage of overall output, application of the principle of proportional responsibility would result in workers' receiving only a tiny fraction of what they are legally due, even where university codes were successfully enforced.

Thus, we must note that in terms of both transparency and remediation, Nike's efforts in this case have been positive and highly beneficial to the workers. At the same time, Nike's work is not done; it is obligated to continued efforts on this case and to ensure that the violations are fully corrected.

#### *Response of Dallas Cowboys Merchandising*

The WRC initially contacted the Dallas Cowboys, along with other licensees, in April 2011 regarding this case.

For several months, the Dallas Cowboys maintained that they had no obligation to take any action to remedy the violations at PT Kizone. The WRC has reported previously to affiliate universities about our concerns with the Cowboys' response.<sup>38</sup> The company's approach drew significant criticism from student activists and other concerned stakeholders.

Ultimately, the Cowboys changed their position and pledged to pay \$55,000 to the PT Kizone employees – an amount the Cowboys say is proportional to their share of the factory's production. This is a step in the right direction. At the same time, the amount involved is obviously very small: less than 2% of the original severance entitlement and an average of roughly \$20 per worker. This provides a useful illustration of the serious practical problems with an approach that limits a buyer's responsibility for remediation to fixing only that portion of the problem commensurate with its share of production. The Cowboys have agreed to work with the DPC to distribute the funds.

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<sup>38</sup> See WRC Update: PT Kizone, June 10, 2011, at: <http://www.workersrights.org/university/memo/061011.html>

## VII. The Impact of the Violations on Workers and Their Families

### *The Implications of the Non-Payment of Mandatory Terminal Compensation in Indonesia*

In considering the impact of failure of an employer to pay severance, it is important to understand the national context. Unlike workers in wealthier countries like the United States, Indonesian workers do not benefit from government-provided income support in the event of unemployment and resulting poverty. There is no unemployment insurance and there are no other income support programs for families and children. The responsibility of protecting workers from the economic devastation in which sudden unemployment can result is assigned, by Indonesian law, to the employer, in the form of mandatory severance and other terminal compensation. When an employer fails to pay workers this legally mandated benefit, workers have no alternate source of support. Moreover, most apparel workers in Indonesia make far too little money to accumulate any significant savings; the regular wage for workers at PT Kizone was approximately 60 cents per hour. Indonesian apparel workers therefore cannot rely on savings to cushion the blow of losing their legally mandated terminal pay. For these reasons, from a labor rights standpoint, compliance with severance requirements is among the most important obligations of employers.

### *Specific Examples of the Impact on Affected Workers*

Over the past month, the WRC surveyed twenty workers about the impact that the failure to pay severance has had on them and their families. The following is a summary of information provided by these workers:

- All of the workers reported that they had difficulty buying sufficient food for themselves and their children. Several had cut their families' meals down to two a day and many had eliminated all meat from their food budget except small local fish.
- When asked how they were dealing with healthcare, most reported that they could only buy over-the-counter medication from a neighborhood vendor; they could not afford to see any kind of medical professional.
- A significant majority of the workers reported that they had gone into severe debt since the factory closed. Whether they were buying food on credit at high interest, falling behind on rent or school fees, borrowing money from neighbors and family members, or all of the above, this weighed heavily on their minds.

The following are examples of information provided by individual workers:

Entis Sutisna, a 45-year-old woman who had worked as a cutting operator at PT Kizone, reported that she has sold all of the saleable goods she could find in her house. A

motorbike that served as her family's transportation was repossessed because she could no longer make the payments. Most damaging to her family's long-term prospects, she has not been able to complete the school payments for the oldest of her three children. (In Indonesia, even public schools require tuition fees, in addition to costs for uniforms and books. School fees were a major source of concern for the majority of the workers interviewed.) While her son has virtually completed his education, the school will not release his diploma unless the payments are made. This will have a serious impact on his ability to find decent work that will enable him to support himself and contribute to the well-being of his mother and younger siblings.

Like most of the workers, Nining, a 40-year-old woman, lives with a spouse who also works. Her husband works in the informal sector as a motorcycle taxi driver, using his motorbike to offer rides to pedestrians. The family is now struggling to pay the motorcycle debt payments, the electrical bill, and school fees. They may lose their motorbike. Like Entis Sutisna, Nining and her husband had been putting their children through school but are now unable to find the money to obtain one child's diploma.

## **VIII. Conclusion**

The workers of PT Kizone and their families have now been waiting for as long as sixteen months to receive the terminal compensation they legally earned. They have suffered substantial hardship as a result of the university code of conduct violations at the factory and it remains urgent that these violations be remedied. This will require further action by the licensees, in particular adidas, which to date has paid nothing to the workers. Without such action, the violations of labor right at PT Kizone will likely never be corrected.