

The Global Reporting Initiative, (GRI) & A Report Regarding a Leading SRI based Ratings Agency

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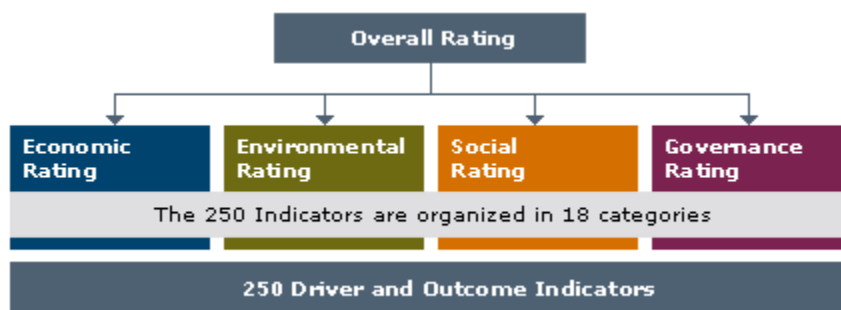
ASSET4: The Problem, An Overview of a typical ESG Ratings Agency

The ASSET4 Integrated Rating Framework is promoted as enabling both professional investors and corporate executives “to integrate extra-financials into mainstream investment and decision making processes systematically and transparently.”¹

Methodology

It is difficult to obtain a clear understanding of the methodology used within the framework as ASSET4, despite basing its framework on the GRI indicators, which are in place to, (it says) encourage greater corporate transparency, provides limited information within its website. However, the website does indicate that the framework relies on the use of publicly available information such as annual reports and company listings, to obtain information on their four “pillars” of financial, environmental, social and corporate governance management.

The framework includes over 250 Driver and Outcome Indicators organised into 18 categories addressing the four pillars. “Driver indicators provide information on management quality, by looking at the different policies, means of implementation and control mechanisms a corporation has in place. They are lead indicators forecasting future outcome. Outcome indicators give a picture of actual performance, performance improvements, transparency and areas with higher than average risk exposure.”²



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ASSET4 developed its list of material and relevant indicators from the nearly 3000 identified within the Global Reporting Initiative (GRI) “Only the most objective indicators of performance, risks, opportunities and reputation were selected for an initial set of possible indicators. Indicators were also only selected if

¹ <http://www.ASSET4.com/page120.html>. December 15, 2006.

² <http://www.ASSET4.com/page130.html>. December 15, 2006.

³ <http://www.ASSET4.com/page130.html>. December 15, 2006.

we could find answers to them for at least 10% of the relevant companies.”⁴ **This practice alone excludes huge numbers of companies from any assessment.**

The indicators are considered to reflect the best management practices possible as the GRI was developed from a multi stakeholder consultation process incorporating expertise from a variety of subject areas. At present there are approximately 850 companies worldwide complying, to various degrees, with the guidelines?⁵

Versions 2 of the GRI Sustainability Guidelines (superseded in October 2006 by Version 3) are considered to have major faults which raise the risk of any rating system being based upon it being significantly flawed.

- **GRI does not have in place a mechanism to ensure the accuracy of the claims within reports by companies who state that they comply with the GRI guidelines.** In fact GRI insists that it is not its role to pass judgement on the quality of information in the reports.

This remains a considerable problem within Version 3 of the guidelines for as GRI continues to say that “it should play no role in certifying reports. But as the numbers using the framework continue to rise; it may have to do more to maintain high standards of disclosure. Or as Markus Reichart, of South African corporate responsibility consultants URS puts it, at some point GRI must “flush out the freeloaders.”⁶

- **The GRI guidelines provide standards for reporting not for performance.** There is no control of the listed firm’s performance. However, given that there is no formal mechanism to certify reports, there is also no mechanism to remove credibility to those companies whose reporting does not match their performance.

Whilst there are now three layers of compliance with the guidelines identified, both versions fail to comment upon how well or how accurately, particular indicators are covered. It remains the responsibility of the companies to self-declare their level although in version 3 there is further advice on doing so. However, even when a company seeks to be accurate in its declarations, this proves difficult as **each reporting company has to make its own definition of the measurement of the indicators and indicators are ambiguous for example, companies within some countries are unable to comply with the guidelines as some national legislation make it illegal to register an employee’s nationality which is sought within the guidelines.**

⁴ <http://www.ASSET4.com/page130.html>. December 15, 2006.

⁵ Russell, J. 2006. Europe special report: the Global Reporting Initiative - GRI's G3 Guidelines - Standards at a crossroads. <http://www.ethicalcorp.com/content.asp?ContentID=4619>. December 18, 2006.

⁶ Russell, J. 2006. Europe special report: the Global Reporting Initiative - GRI's G3 Guidelines - Standards at a crossroads. <http://www.ethicalcorp.com/content.asp?ContentID=4619>. December 18, 2006.

The guidelines have been criticised as indicators are ‘narrative’ describing policies and procedures without any mechanism to ensure that the policy and procedures are followed in practice.

Claims as to the widespread nature of stakeholder consultation are also not unproblematic. **Historically the GRI organisation has been mainly financed by business which inevitably prioritised business interests rather than social and environmental interests. More recently “voices from the financial markets – including representatives of FTSE, Goldman Sachs and UBS – played an influential role in developing the guidelines.** This willingness and interest from investors to be involved was absent four years ago, observes Ernst Ligteringen, GRI chief executive. And their demands are reflected in the new guidelines, he says.”⁷

Examination of the GRI’s Stakeholder Council Members, Board of Directors and Stakeholder Organisations shows a clear bias for industry, SRI institutions both financial and consultative and lacks any significant representation from the international world of certification such as ISO, WTO, etc.

Further in September 2006, the Financial Times obtained a report commissioned by the UN Environment Programme, a GRI supporter since 1998 and written by the Global Public Policy Institute, a Berlin-based think-tank raised significant concerns about the likely levels of company reporting on social and environmental impacts in the future. The study considered that “non-financial reporting” in the future would only play “a ‘very limited role in sustainable development” with such reporting limited “to transnational companies based in industrial countries.”⁸

Corporate social responsibility advocates who consider the reporting of non-financial issues to be core to efforts to improve such practices will view the prediction that “by 2020 only 11 per cent of transnational companies - let alone other businesses - will provide social and environmental data”⁹ with dismay.

Despite the flaws described above, ASSET4 has developed its rating framework by adapting the GRI indicators in such a way as to obtain ‘quantitative’ indicators. Vice President of Marketing and Business Development, Henrik Steffensen¹⁰ comments that they take “information and quantify it; we take qualitative statements and turn them into quantifiable data.”

The article (hosted on the website of ASSET4) by Martin Hurst for *Investment and Pensions Europe* describes the methodology and considers that ASSET4;

“Provide information on management quality by looking at the different policies, implementation, monitoring and improvements...These are what ASSET4 terms ‘lead indicators forecasting future

⁷ Russell, J. 2006. Europe special report: the Global Reporting Initiative - GRI's G3 Guidelines - Standards at a crossroads. <http://www.ethicalcorp.com/content.asp?ContentID=4619>. December 18, 2006.

⁸ Williamson, H. 2006. *The Americas and International Economy: UN fears decline in non-financial reporting*. FT. <http://search.ft.com/searchArticle?queryText=GRI&y=0&javascriptEnabled=true&id=060925000932&x=0>. December 18, 2006.

⁹ Williamson, H. 2006. *The Americas and International Economy: UN fears decline in non-financial reporting*. FT. <http://search.ft.com/searchArticle?queryText=GRI&y=0&javascriptEnabled=true&id=060925000932&x=0>. December 18, 2006.

¹⁰ Hurst, M. 2006. *SRI/Governance Driving the Outcome*. Investment and Pensions Europe. March 2006. Pg 62. <http://www.ASSET4.com/page230.html>. December 15, 2006

outcomes.’ These are typically points requiring yes/no answers, for example; does the company under review have an environmental policy?’¹¹

Probus considers that the weakness of this approach is demonstrated within the ASSET4/GOE report, *The Relation Between Sustainability Performance and Financial Performance of Firms*. The report describes it’s quantification of the GRI.

“Qualitative indicators were reformulated such that they could be answered with either a ‘yes’ or ‘no.’ As a clarifying example, consider the question ‘What are the main issues for the organisation related to the major themes of sustainable development?’ ...This question was reformulated as follows: ‘Does the organization report on its main issues with respect to the major themes of sustainable development?’. Qualification was achieved by assigning all ‘yes’ answers a value of 1 and all ‘no’ answers a value of ‘0’. ”¹²

Whilst this process provides a quantitative score, it is one premised upon a number of subjective considerations. For example who has decided what the ‘main issues’? are? What level of expertise do they process to make this decision? What are the main themes of sustainable development? How is the quality of an environmental report assessed? This approach leaves both the company assessed and the rating system vulnerable to accusations of ‘greenwash.’

The weaknesses in the ASSET4 approach are apparent. For example, in embedding itself within the GRI approach, it is inevitably linking itself to the Corporate Social Responsibility methodology of company self-reporting, which is unreliable. Whilst companies “that form ASSET4’s universe have the opportunity to verify the information that is collected and fill in the gaps where information is missing”¹³ there is no information to suggest that any information gained has received third party endorsement. Of course if relying on financial statements of companies these will have received third party audit by financial auditors. However, these auditors are not generally qualified to assess the social, environmental and corporate governance claims of companies.¹⁴

¹¹ Hurst, M. 2006. *SRI/Governance Driving the Outcome*. Investment and Pensions Europe. March 2006. Pg 62. <http://www.ASSET4.com/page230.html>. December 15, 2006

¹² Weber, O. Dr et al, 2005. *The Relation between Sustainability Performance and Financial Performance of Firms*. GOE & ASSET4. http://www.vfu.de/scin/userdata/File/Downloads/roundtable%202005/GRI_Report.pdf. December 15, 2006. Pg 8.

¹³ Hurst, M. 2006. *SRI/Governance Driving the Outcome*. Investment and Pensions Europe. March 2006. Pg 62. <http://www.ASSET4.com/page230.html>. December 15, 2006.

¹⁴ Ernst & Young were subjected to criticism when they were found to have unjustly accepted Nikes claims regarding its practices. O’Rourke, D. 1997. A Critique of Nike’s Labor and Environmental Auditing in Vietnam as performed by Ernst & Young. <http://www.corpwatch.org/article.php?id=966>. December 18, 2006.

Therefore, despite ASSET4's claims that they evaluate "a company by means of a very clear and methodical process against each of the indicators that it tracks" using a "scientifically validated and model-based evaluation,"¹⁵ the publicly available information to date does not support this claim.

Clearly ASSET4 have developed persuasive and effective documentation detailing considerable claims which given their start-up costs of SFr 8.5 million as of October 2005¹⁶ & ¹⁷ is not surprising. Nor is the fact that in June 2006 Goldman Sachs licensed ASSET4 extra-financial information and took up a stake in its financing.¹⁸

ASSET4 states that they have established the "largest database of corporate extra-financial information and the tools necessary to track, analyse and benchmark that data,"¹⁹ However, in June 2006 they had 700 companies within its universe and whilst seeking to reach more than 1200 companies by the end of 2006 and all 3000 organisations within the MSCI World Index. (Morgan Stanley Capital International)²⁰ in due time, this is not significantly larger than that held by Probus.

It may prove that rather than providing an objective and effective measurement of a company's environmental, social, financial and corporate governance practices, ASSET4 may have developed a useful software platform providing data to both company executives and investment executives which they can access and manipulate. For example

"ASSET4 provides no interpretation of the data, and is a result of a range of multivariate statistical analysis methods comparing companies' financial performance with their performance in the extra-financial areas. The result is a model-based objective rating that enables users to systematically benchmark and access corporate performance, as well as use their expertise to interpret the information provided. In fact, users may change the weightings of the criteria or leave out aspects they feel are not relevant to their specific assessment. Users are thereby empowered to customise the evaluation to reflect their individual values or to focus on themes of particular importance and interest."²¹

¹⁵ <http://www.ASSET4.com/page140.html>. December 15, 2006.

¹⁶ Thompson, V. 2005. Private equity column October. <http://swissventures.blogspot.com/2005/10/private-equity-column-october.html>. December 18, 2006.

¹⁷ This figure is confirmed by Alarm: Clock Euro. 2006. *Ohnemus' ASSET4 Taps Goldman Sachs As Strategic Partner* http://www.thealarmclock.com/euro/archives/2006/06/ohnemus_ASSET4_venture_taps_go_1.html. December 15, 2006.

¹⁸ <http://www.ASSET4.com/page220.html#gs>. December 15, 2006.

¹⁹ <http://www.ASSET4.com/> December 15, 2006.

²⁰ <http://www.ASSET4.com/page220.html#gs>

²¹ <http://www.ASSET4.com/page140.html> December 15, 2006.

Whilst this provides a useful service to clients, such manipulations do not enable an objective and scientific analysis to be conducted.

A detailed description of ASSET4's software platform is available at <http://www.ASSET4.com/page130.html>.²² Certainly the company has developed useful software platform which Goldman Sachs considers of value. It may prove of note that ASSET4's co-founder, Peter Ohnemusone, co-founded The Fantastic Corporation, a Swiss software company that wanted to enable broadband content delivery from creator to customer.²³

In conclusion, despite ASSET4's claims, it is our opinion that ASSET4 is embedded within SRI/CSR methodology, (the inaccuracy of which will increase exponentially) cannot provide objective and measurable data for the financial markets. It may provide the largest database to date of company information although this lead is likely to be short-lived. However, as the Integrity Research Associates comment in their article *SRI Research Going Mainstream?* SRI is becoming more mainstream as demonstrated by the Goldman Sachs collaboration with ASSET4; it has yet to "become a much more robust and profitable research practice"²⁴

HISTORY REPEATS ITSELF, IS THIS WHY BP EMPLOYED E&Y?

This is a Report from 1997 following the first major ESG related corporate disaster, Stock holders lost \$ Millions and the Nike Brand took a long time to recover.

We find it interesting that knowing this BP would elect to have E&Y Audit their environmental compliance and internal standards.

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²² It is of interest that the only reference to any internationally agreed standard within their documentation and website relates to IBM xSP Prime Hosting certified partner, which it states is "the best possible IBM hosting certification. This certification means that specific requirements based on ISO9000 audits, relating to data security, system availability, capacity and scalability, have been fulfilled." However, a search of the IBM website was unable to identify details of this certification although it is apparent that IBM has a number of personal certification programmes which they provide. (<http://www.ibm.com/us/>)

²³ Alarm Clock Euro. http://www.thealarmclock.com/euro/archives/where_are_they_now/. December 15, 2006.

²⁴ Integrity Research Associates. 2006. *SRI Research Going Mainstream?* Equity Research News. http://integrityresearch.blogdrive.com/archive/cm-11_cy-2006_m-11_d-15_y-2006_o-0.html. December 15, 2006.

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About the Author

Dara O'Rourke is a research associate at the Transnational Resource and Action Center (TRAC), and a consultant to the United Nations Industrial Development Organization (UNIDO) in Vietnam. His research focuses on strategies for preventing adverse environmental and social impacts of industrial activities. He has been conducting research in Vietnam for the last three years. Mr. O'Rourke has worked as a consultant to the United Nations Environment Programme, the World Bank, and the U.S. Environmental Protection Agency. Mr. O'Rourke has a Bachelor's degree from the Massachusetts Institute of Technology in Mechanical Engineering and Political Science, and a Master's degree from the Energy and Resources Group at the University of California, Berkeley. He is currently completing his Ph.D. at Berkeley.

About Transnational Resource & Action Center (TRAC)

TRAC works to help build global links for social justice, ecological sustainability and corporate accountability. Its web site, Corporate Watch --- www.corpwatch.org ---, provides news, information, and analysis for the general public about the role corporations play in social political, economic and environmental issues in the U.S. and around the world. TRAC is a project of The Tides Center.

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Exclusive photographs, the first independent pictures taken inside a Nike factory in Vietnam, will be available on the Corporate Watch Web Site after November 10th. This report and the entire Ernst & Young Audit will also be available.

Forward

As public scrutiny of sweatshops in the apparel industry continues to grow, one of the central issues under discussion is how the global operations of U.S. corporations such as Nike can best be monitored to certify decent and healthy working conditions.

Indeed, the White House Apparel Industry Partnership, which is due to make a series of recommendations to President Clinton in November, is currently debating two sides of this question. On the one hand, corporations on the task force such as Nike argue that accounting firms like Ernst and Young are best qualified to serve as monitors by carrying out labour and environmental audits. On the other hand, labour, religious and human rights organizations insist that independent, publicly accountable monitors would be best qualified to undertake this task.

This debate, however, has been fundamentally flawed by the fact that the public, and most of the members of the task force, have never seen an audit of labour or health and safety conditions produced by an accounting firm.

TRAC is pleased to be able to shed some light on this subject by releasing the first audit of this kind ever to be made public: a confidential Ernst and Young assessment of the Tae Kwang Vina plant, a factory which employs 9,200 workers who produce 400,000 pairs of shoes a month exclusively for Nike in Vietnam.

We are also happy to make public the first photos independently taken inside a Nike plant in Vietnam.

Furthermore, we are proud to publish TRAC Research Associate Dara O'Rourke's report, *Smoke From A Hired Gun*, an analysis and critique of the Ernst and Young audit.

Mr. O'Rourke is a consultant to the United Nations Industrial Development Organization (UNIDO), and has conducted research in over 50 factories in Vietnam. One of them was the Tae Kwang Vina factory, a Nike subcontractor in the Dong Nai province of Vietnam, and the subject of the Ernst and Young audit. Mr. O'Rourke visited this factory three times in 1997. During the visits to the plant, he performed walk-through audits of environmental and working conditions, interviewed management personnel, met with Tae Kwang Vina's managing director, and with representatives of Nike Inc. in Vietnam. He also interviewed workers confidentially outside the factory--something that Ernst and Young failed to do.

Ernst and Young found Nike's subcontractor to be in violation of a number of Vietnamese labour and workplace environmental laws. This finding is in contradiction to Ernst & Young's own conclusion that Tae Kwang Vina is in compliance with the Nike "Code of Conduct."

Furthermore, Mr. O'Rourke found Ernst and Young's methodology to be highly deficient, having ignored "most accepted standards of labour and environmental auditing." Mr. O'Rourke's assessment, including his interviews with workers, reveals a far worse situation in the Nike plant than Ernst and Young portrays.

Indeed, Ernst and Young's incompetence as a social and environmental auditor combined with Mr. O'Rourke's own findings inside the plant, present a strong argument against using accounting firms to conduct labour and environmental audits.

We hope these reports will serve as a constructive contribution to the effort to eliminate sweatshops around the world.

China Brotsky, Chair of the Board, Transnational Resource & Action Center (TRAC)

Joshua Karliner, Executive Director, Transnational Resource & Action Center (TRAC)

Executive Summary

The Ernst & Young Audit

- A confidential Ernst & Young audit of labour and environmental conditions inside a Nike factory in Vietnam was recently leaked to the Transnational Resource & Action Center (TRAC).
- This is the first time that an accounting firm's labour and environmental audit of any apparel company has ever been made public.
- The question of whether firms such as Ernst & Young are competent to monitor the shoe and garment industry is currently under discussion by the White House Apparel Industry

Partnership.

- An examination of the Ernst & Young audit raises serious questions about the legitimacy and competence of accounting firms' as independent monitors of labour and environmental issues.
- TRAC is also releasing the first photos taken independently inside a Nike factory in Vietnam.
- The Ernst & Young audit also sheds light on, and raises questions about the findings of Andrew Young, the former UN Ambassador hired to evaluate Nike's "Code of Conduct."

Ernst & Young on the Conditions inside this Nike Factory

- The Ernst & Young report, which Andrew Young claimed to have access to, shows that Nike's "Code of Conduct," even when followed, allows dangerous working conditions to persist in its plants.
- Although flawed in a number of ways, the audit notes continuing violations of labour laws on maximum working hours, unprotected chemical exposures, poor treatment of workers, and management control of the trade union.
- Among the factory's 9,200 workers who produce 400,000 pairs of mid- to high-end Nike shoes per month, the audit reports high levels of respiratory illnesses in sections with high chemical use.
- The audit determined that even though Tae Kwang Vina Company (the subcontractor in question) violates Vietnamese labour and environmental laws, it is at the same time in compliance with Nike's "Code of Conduct."
- Tae Kwang Vina is reportedly the most technically advanced of Nike's subcontractors in Vietnam.

TRAC's Findings on the Conditions inside this Nike Factory

Confidential interviews with employees outside of the factory provided information about numerous violations of Nike's Code of Conduct that were not discovered by the Ernst & Young audit, including:

- Violations of Vietnamese labour laws on pay;
- Violations of Vietnamese labour laws on maximum overtime hours;
- Forced overtime;
- Strike breaking; and,
- Physical and verbal abuse of workers.

Shortcomings of the Ernst & Young Audit

- The audit is missing information regarding occupational health and safety, environment, and general working conditions.
- The methodology employed by Ernst & Young ignores most accepted standards of labour and environmental auditing. For example, the audit involved no monitoring or sampling of air quality in the factory.
- Most of the data came directly from management sources.
- The audit overlooks many of the key issues of concern in Nike plants around Asia, including: physical and verbal abuse of workers, sexual harassment, repercussions for attempts to organize, and contract violations.

Relevance to the White House Task Force

- This audit highlights how important issues can be covered up or ignored in "independent monitoring." Some form of public disclosure is critical to insuring the quality of auditing.
- The audit provides a strong argument against using accounting firms to conduct labour and environmental audits.
- The poor quality of this audit argues for truly independent monitoring of Nike plants. Labour, religious, or human rights organizations that pass an accreditation program would be more appropriate auditors.

Background -- Nike in Asia

Nike, Inc., the world's largest retailer of athletic shoes, has come under increasing criticism recently over working conditions in its factories in Asia. Labour and human rights groups have reported physical and verbal abuse of workers, hazardous working conditions, pennies per hour wages, and anti-union efforts throughout Indonesia, China, and Vietnam, where Nike employs over 350,000 workers.¹ Nike's treatment of its workers stands in stark contrast to the record \$795 million in profits it reported this year.²

Nike initially responded to public criticisms by claiming no control over the conditions inside the factories making its shoes and clothing. Nike argued that as the company does not own any of the factories producing its products, Nike could not influence the working conditions or pay.³ Labour rights groups have challenged this claim, demanding that Nike take responsibility for its subcontractors' actions.

Nike has since changed its strategy. First it hired two public accounting firms, Ernst & Young and Price Waterhouse, to perform internal audits of the labour and environmental practices inside its subcontractors. Nike describes the Ernst & Young audits as "systematic, unannounced evaluations by independent auditors"⁴ of current working conditions inside their factories.

Second, it hired former UN-Ambassador Andrew Young's consulting firm GoodWorks International LLC, to review the company's "Code of Conduct" and subcontractor compliance. Andrew Young's report, which largely exonerated Nike, was made public and followed up with a PR campaign. The much more in-depth internal audits however, which Andrew Young claimed to have access to, have remained completely confidential.

These "independent audits" are now central to debates around improving conditions inside the globally dispersed subcontractors of US firms. A White House commission is currently examining the issue of independent auditing.⁵ Nike and other apparel companies in the commission argue that corporations should be able to employ their own accounting firms to perform these audits. Labour, religious, and human rights groups however, disagree, arguing that truly independent auditing is critical to the task of ending sweatshops around the world. A truly informed discussion of the issue has been limited by the fact that audits by these accounting firms have never been made public.

Until now, without evidence on the quality of accounting firm audits, it was impossible to determine whether these firms could, or would, do an adequate job of labour and environmental auditing. However, just this month, an Ernst & Young audit of one Nike subcontractor - the Tae Kwang Vina Company, a Korean manufacturer operating in Vietnam - was leaked to TRAC. Tae Kwang Vina employs 9,200 workers, and produces more than 400,000 pairs of Nike's mid- to high-end athletic shoes per month. This audit offers a rare opportunity to examine the methodology, findings, and recommendations of an industry auditor.

The Ernst & Young Methodology

While their methodology is not explicitly presented, Ernst & Young explain that "the procedures we have performed were those that you [Nike] specifically instructed us to perform. Accordingly, we make no comment as to the sufficiency of these procedures for your purposes." As this statement makes clear, Ernst & Young did not perform an "independent" audit, but rather simply followed Nike's instructions.

The Ernst & Young auditors spent approximately one week in the Tae Kwang Vina factory.⁶ They relied largely on management information about working conditions, organizational practices, and wages to write their report. They performed no environmental monitoring or air sampling of their own. Occupational health and safety information came entirely from secondary sources (largely Vietnamese government agencies). Information on worker perceptions and attitudes came from a survey of 50 employees "randomly selected...from the payroll register."

The Ernst & Young report, taken on its own, is poorly written, fraught with errors, and convoluted in structure. As discussed below, the audit methodology and reporting fail to adhere to the conventions of occupational health and safety, or environmental auditing. Ernst & Young's audit procedures appear simply to be based on Nike's instructions.

Issues Revealed by the Ernst & Young Report

Despite methodological flaws, the report does come to a number of striking conclusions about the working conditions inside Tae Kwang Vina. These include:

Chemical Exposures

- From a "sample of 165 employees from Mixing, P.U., Roller sections, there are 128 employees (77.57%) getting respiratory disease..." (E&Y Page 9. References in this section are to the Ernst & Young Report which is included as an Appendix.)
- "Dust in the Mixing Shop exceeded the standard 10 times." (E&Y Page 8) This dust includes resins that are potentially very hazardous because they cause respiratory ailments.
- Toluene concentrations "exceeded the standard from 6 to 177 times" in several sections of the factory. (E&Y Page 8) Toluene is a chemical solvent that is known to cause central nervous system depression, damage to the liver and kidneys, and skin and eye irritations.
- Chemical releases have led to an "increasing number of employees who have disease [sic] involving skin, heart, allergic, [and] throat working in chemical involved sections." (E&Y Page 8)
- Acetone concentrations "exceeded the standard 6 to 18 times." (E&Y Page 8)

Lack of Safety Equipment and Training

- "Personal protective equipment (gloves, masks) are not daily provided. (E&Y Page 4) Workers "do not wear protective equipment...even in highly-hazardous places where the concentration of chemical dust, fumes exceeded the standard frequently." (E&Y Page 6)
- "There are [sic] no training on proper handling of chemicals for related employees in daily exposed [sic] to chemicals." (E&Y Page 6)

Working Conditions

- Workers are punished or fined for "violating code of section such as talking during working hours." (E&Y Page 3)
- "40 workers [out of 50] do not read NIKE's Code of Conduct [and] even do not know exactly what NIKE is." (E&Y Attachment II, Page 2)
- "48 cases [out of 50] where workers were required to work above the maximum working hours." (E&Y Page 2)

It is interesting to note that even with these findings Andrew Young concluded that Nike was doing a "good job." This would indicate that either Andrew Young was not shown all of the internal audits Nike commissioned, or he has a very different view of a "good job" than would most occupational health and safety specialists.

Biases in the Audit

The Ernst & Young audit methodology results in biased findings on a number of critical issues. For example, posing a question about pay without guaranteeing protection from repercussions, can discourage candid answers, and is likely to lead to a biased analysis. As a consultant to the United Nations Industrial Development Organization in Vietnam, I visited the Tae Kwang Vina plant three times during 1997. I also interviewed workers in confidence away from the factory. My research paints a very different picture than the Ernst & Young audit.

Ernst & Young asserts:

"40 workers [out of 50 interviewed] are satisfied with their salary," which officially starts at \$40 per month, although new workers are paid a lower "training wage". (E&Y Attachment 2, Page 2)

TRAC:

This finding highlights one of the problems with Ernst & Young's interview method. In my research, not one of the workers I spoke with at Tae Kwang Vina (including office staff) was "satisfied" with their pay.

Ernst & Young:

"46 workers opined that working overtime hours are acceptable while 4 workers do not appreciate working overtime." (E&Y Attachment 2, Page 2)

TRAC:

This statement ignores the deeper rationale for working overtime - base salaries are extremely low. Tae Kwang Vina pays one of the lowest base salary of any of the 50 large factories I have studied in Vietnam.

Ernst & Young:

Only "15 workers are not satisfied with the working conditions (hot, stuffy)." (E&Y Attachment 2, Page 2)

TRAC:

The workers I spoke with complained about working conditions, including heat, chemical exposures, poor ventilation, forced overtime, and verbal abuse by managers.

Ernst & Young:

"There's a high rate of labour accidents caused by carelessness of employees." (E&Y Page 7)

TRAC:

A serious occupational health and safety audit would analyse the underlying causes of accidents - such as the absence of training and hazard prevention programs - rather than simply blaming the victims. To

attribute accidents to carelessness rather than working conditions without thorough analysis is another example of bias in the audit.

Ernst & Young:

The audit notes that "the workers trade union is still being organized by the management and the workers." (E&Y Page 2)

TRAC:

Workers report that leaders of the trade union were selected and paid by Tae Kwang Vina's management.⁷

What Ernst & Young Missed

In my interviews with employees, I was given information about numerous violations of Nike's Code of Conduct that were not discovered by the Ernst & Young audit. I was informed that managers of Tae Kwang Vina have:

- Violated Vietnamese labour laws on maximum overtime hours. Night-shift workers in the stitching section told me that their "standard" work week is 10.5 hours per day, six days per week. This basic work week can lead to 700 or more overtime hours per year, well over the legal maximum of 200 overtime hours per year.;
- Forced overtime. Workers complained that they have no choice in whether or not they work overtime. Workers are told one day in advance that they must work overtime. If they "choose" not to work overtime more than twice, they are likely to be fired.
- Violated Vietnamese labour laws on pay. Tae Kwang Vina is required to pay increasing wages based on workers' skills. Workers at skill level 1 should be paid the minimum wage (\$40/month) times a multiplier, skill level 2 should be paid \$40 times a higher multiplier, etc. One staff member told me the company ignores this legal requirement, giving annual salary increases much lower than required.
- Broken strikes. Tae Kwang Vina management have repeatedly threatened to fire all workers who wouldn't return to work during strikes over the last two years. An office staff member explained that "managers investigate who incited the action, and don't fire them, but make them change jobs, and treat them very badly until they quit."
- Physically and verbally abused workers. I was told numerous stories about managers hitting workers. Reportedly, in one case the director of security hit a Vietnamese guard. In another case, a manager hit several women workers with a broom while trying to force them to leave the factory in a single file line.

- Sexual harassment. Several workers told me that a Korean manager allegedly attempted to rape two women workers last year, and then fled the country. This was widely reported in the Vietnamese press.⁹ Independent monitors on the ground in Vietnam would have been aware of this case and would have followed up on these issues.

Tae Kwang Vina is the most technically advanced of Nike's subcontractors in Vietnam, and according to Nike is no worse on labour or environmental issues than the other four Nike factories in Vietnam.¹⁰ In fact, Tae Kwang Vina received the highest score of Nike's five factories in Vietnam in a self-assessment procedure.¹¹

The serious omissions and biases in the Ernst & Young findings point out the weaknesses of using accounting firms to audit labour and environmental practices. These auditors are not trusted by workers, and their findings are never submitted to public scrutiny.

What Ernst & Young Should Have Analysed

In following Nike's instructions for the audit, Ernst & Young failed to comprehensively analyse labour and environmental conditions inside the Tae Kwang Vina factory. The audit is missing important information regarding occupational health and safety, environment, and general working conditions. An audit should be designed to determine normal operating practices within a factory, to evaluate recognized hazards and how they are controlled, and to analyse how new hazards are identified and controlled.¹² In order to do all this, auditors need to be trained in hazard recognition, and must be able to independently assess management actions. Ernst & Young failed to adequately analyse both existing hazards and procedures for resolving new hazards.

An Industrial Hygienist who performs worker health and safety compliance inspections for the State of California¹³ noted that if Tae Kwang Vina had been operating in the U.S., it would have been cited and fined on numerous counts, including:

- chemical over-exposures;
- inadequate ventilation;
- noise over-exposures;
- lack of personal protective equipment;
- absence of a hazard communication program;
- lack of job-specific training for operating machinery; and,
- lack of drinking water in high heat stress environments.

The Ernst & Young audit failed to examine any of these issues in detail, and ignored exposures to other hazardous chemicals such as Methyl Ethyl Ketone and glues in the plant. The audit also failed to examine

why employees with respiratory illnesses were still working in areas of exposure without controls, and why no safety committee exists in a factory with 9,200 workers.

The audit should have also examined issues that are common points of concern in Nike plants around Asia, and that have been specifically raised at the Tae Kwang Vina plant. Workers should have been interviewed off-site with guaranteed anonymity regarding physical and verbal abuse by managers, sexual harassment, general working conditions, and pay issues. Lora Jo Foo, Managing Attorney for the Asian Law Caucus and President of Sweatshop Watch, asserts that "it is impossible to do an analysis of minimum wage or overtime compensation without having information on the actual hours worked, and the take-home pay of the workers, both of which were missing from the Ernst & Young audit. A proper analysis would involve unannounced monitoring of working hours, and interviews with workers away from the factory."¹⁴

The environmental section of the Ernst & Young audit similarly misses most of the key environmental issues in this factory. At a minimum the audit should have listed all chemicals used in the plant, noted that burning scrap rubber in the factory's boilers is violating Vietnamese environmental laws, and proposed alternatives to burning rubber.

A truly independent audit of labour and environmental practices would involve a more complete analysis of the system within the factory which affects working conditions, health and safety, and the environment. This includes: management policies and actions, company organization, worker training, hazard prevention programs, and existing and potential physical and mental hazards. A long-term auditing program would also include comprehensive health studies of workers in hazardous sections of the plant. This type of audit obviously requires well trained auditors that are committed to independent analysis of the conditions inside the factory.

Conclusions

Dusty Kidd, Nike's Director of Labour Practices, proclaims that Nike will "Assure best practices in every factory where NIKE products are made, regardless of who owns the factory, or the scale and duration of our presence there."¹⁵ Furthermore, Nike claims that "When NIKE leads, others follow. We're the leader -- always have been, always will be."¹⁶ Despite these bold claims, the leaked Ernst & Young audit provides evidence that working conditions can hardly be described as "best practices" in a factory which is said to be Nike's most technically advanced plant in Vietnam.

The Ernst & Young audit also presents a strong argument that accounting firms retained by manufacturers are not the appropriate organizations to be conducting audits of labour and environmental conditions. Accounting firms such as Ernst & Young simply do not have the training, independence, or the trust of workers, to perform comprehensive, unbiased audits of working conditions. We agree with a State of California health and safety compliance officer who argues in an industry newsletter that "putting the fox's paid consultant in charge of the hen house" is not the solution.¹⁷ It is also clear from the leaked audit that Andrew Young's report on Nike failed to examine

many of the critical issues related to labour and environmental conditions in Nike plants.

The information presented in this audit represents only the tip of the iceberg of poor working conditions inside Nike and other US subcontractor factories around the world. For instance, there have been widespread reports in the Vietnamese press about similar conditions in other Nike plants.¹⁸ A recent investigative report from China documents serious problems in Nike and Reebok plants there.¹⁹ Nike's Indonesian factories have been criticized for their mistreatment of workers for years.²⁰

If Nike genuinely wishes to improve the conditions inside its plants, it would, as the saying goes, "Just Do It." The company should make public all of the internal audits conducted to date. This would shed light on current conditions in its plants, and increase the public's belief that Nike is making a good faith effort to improve.

Clearly only well-trained, independent auditors can perform the types of audits that are needed in Nike's factories. As The New York Times admits, a better alternative to accounting firms would be "local, truly independent monitors who speak the language, can make unannounced visits and enjoy the trust of a largely young, female...workforce."²¹ Labour, religious or human rights groups that pass an accreditation program would be the best candidates for this job.

Endnotes

1. Dottie Enrico, "Women's Groups Pressure Nike on Labour Practices," USA TODAY, October 27, 1997, Pg. 2B; Jon Frandsen, "Nike Invited to Answer Charges of Third World Exploitation," Gannett News Service, October 24, 1997; Brad Knickerbocker, "Nike Fight s Full-Court Press on Labor Issue," The Christian Science Monitor, September 23, 1997; Jonathan Make, "Critics: Young Report Just Doesn't Do It," Business Journal-Portland, June 27, 1997.
2. PRNewswire, "Nike Reports Record Fourth Quarter and Fiscal 1997 Earnings," July 1, 1997, Beaverton, Ore.
3. Donald Katz, Just Do It: The Nike Spirit in the Corporate World, New York: Random House, 1994. Katz quotes one Nike representative as saying "We don't pay anybody at the factories and we don't set policy within the factory; it is their business to run."
4. See Nike's web page www.nikeworkers.com.
5. The Apparel Industry Partnership was created by the White House in August 1996. In April 1997, the Partnership presented the President with a Code of Conduct and Principles of Monitoring. The Partnership plans to release a second report in November 1 1997.
6. Personal communication with Nike staff in Ho Chi Minh City, Vietnam, October 3rd, 1997.
7. Interview with Tae Kwang Vina employee, October 7, 1997.

8. Interviews were conducted with five Tae Kwang Vina employees in October, 1997. These employees ranged from high-level office staff to factory workers.
9. The Worker Newspaper (Nguoi Lao Dong), in Vietnamese, August 23, 1996. See also Duc Hung and Huong Lam, "Foreign Bosses Blasted: Labour Force Abused as Firms Seek Short Cut to Quick Buck," Vietnam Investment Review, Ha Noi, March 3-9, 1997.
10. Personal communication with Nike staff in Ho Chi Minh City, Vietnam, October 3rd, 1997.
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12. Arthur Reich, "Workplace Inspection & Worker Protection," in J. LaDou (ed.) Occupational Health & Safety, Itasca, Illinois: National Safety Council, Second Edition, 1994, PP: 121-161. Elizabeth Gross and Elise Pechter Morse, "Evaluation," in B.A. Pl og, J. Niland, and P.J. Quinlan (eds.) Fundamentals of Industrial Hygiene, Itasca, Illinois: National Safety Council, Fourth Edition, 1996, PP: 453-483.
13. Personal communication with Garrett Brown, MPH, Industrial Hygienist, Nov. 2, 1997. Mr. Brown is a compliance inspector for the State of California, and is the National Coordinator of the Maquiladora Health and Safety Support Network.
14. Personal communication with Lora Jo Foo, October 31, 1997.
15. See Nike's web page www.nikeworkers.com.
16. Ibid.
17. Garrett Brown, "The Slippery Slope of Third-Party Reviews," The Synergist, September 15, 1997.
18. Articles in Vietnamese and English are available from Vietnam Labor Watch or on their web site at: <http://www.saigon.com/~nike/>
19. The Asia Monitor Resource Centre and the Hong Kong Christian Industrial Committee, "Working Conditions in Sports Shoe Factories in China Making Shoes for Nike and Reebok," Hong Kong, September 1997.
20. David Moberg, "Just Doing It: Inside Nike's New-Age Sweatshop," L.A. Weekly, June 20, 1997. Jeff Ballinger, "Just Do It - or Else: Unfair Labor Practices Among Nike Inc.'s Foreign Suppliers," Multinational Monitor, v16, n6, June 1995.
21. New York Times, "Watching the Sweatshops"