WORKER RIGHTS CONSORTIUM

To: WRC Affiliate Colleges and Universities
From: Scott Nova and Jessica Champagne
Re: Remediation of Severance Pay Violations at MDR/CCC (El Salvador)
Date: April 29, 2015

This memorandum summarizes the remediation achieved by the Worker Rights Consortium and other stakeholders following violations that occurred at Manufacturas del Rio (MDR) and the Central American Cutting Center (CCC), two factories housed in a single location and located in the El Pedregal Free Trade Zone in El Salvador. In January 2014, the two companies, both of which operated as part of the Argus Group, unexpectedly closed down, resulting in the immediate dismissal of approximately 1,200 workers. The Argus Group gave workers no advance notice of the closure. Workers were left without their salary for their final week of work and without US$1.8 million dollars in severance and other terminal benefits owed to them in accordance with Salvadoran law.

At the time that MDR/CCC closed, the factory was producing university-licensed apparel for Russell Brands, which is owned by Fruit of the Loom, and non-licensed apparel for Hanesbrands, Lacoste, and Levi Strauss & Company. Levi Strauss reports that the Levi product at MDR/CCC was being produced by a licensee, Hampshire.

The WRC investigated this case following a complaint from two unions that represented the workers at MDR and CCC. After extensive engagement by the WRC with the factory's key customers, who in turn pressed the Argus Group to provide further funds to the workers, a partial payment of these funds totaling US$650,000 was made to workers by the Argus Group in late July 2014, almost six months after the factory closed its operations. An additional US$1.1 million, provided primarily by Hanesbrands and Fruit of the Loom, is currently being distributed to workers, in a process that began on April 27, 2015. The Levi licensee Hampshire also provided a small contribution that will be included in this distribution. Lacoste was alone among the factory's major buyers in failing to make a contribution towards the workers' severance pay.

5 Thomas Circle NW Fifth Floor Washington, DC 20005
(202) 387-4884 Fax: (202) 387-3292
wrc@workersrights.org www.workersrights.org

The distribution underway at this time will make the workers whole for the nominal amount they were denied when the factory closed in January 2014. In cases in which workers have been denied funds to which they were legally entitled for an extended period of time, the WRC always considers interest to also be part of the necessary remedy. Workers have made an involuntary "loan" to the company, and in many cases workers report that they have had to take out loans, generally from local loan sharks charging exorbitant rates, in order to cover their household needs during the period that they were denied the funds that they were owed. In this case, workers have not yet received a payment of interest. However, the WRC is optimistic that the workers will receive additional funds from the sale of the company's assets, which is being implemented by the Salvadoran government. Given this, the WRC considers the case closed with respect to Hanesbrands and Fruit of the Loom.

Failure to provide legally required severance at the time of factory closures remains a common violation in the industry, and one with a particularly serious impact on workers. When factories close, if severance pay is not provided, workers find themselves unemployed, generally with no government-provided safety net, and denied the funds that were intended to support them while they sought a new job. In recent years, the WRC has seen an increasing number of cases in which licensees have acknowledged their responsibility to ensure that workers are made whole in such cases.

The following sections of this memo provide further detail regarding the remediation of the failure to provide severance pay and summarize violations of freedom of association related to the factory closure.

Unpaid Salary and Severance

On January 7, 2014, employees reported to work at MDR/CCC following the factory's annual holiday shut down to find a sign posted at the factory gates informing them that the factory was closed. Workers were not provided with any further details regarding the closure or the funds they were legally owed.

The MDR/CCC workers protested the closure. Over the past decade, workers had formed two unions at the plant. One union is affiliated to the Sindicato de la Industria Textil (STIT). The other, the Sindicato de Trabajadoras y Trabajadores de la Empresa Manufacturas del Rio (SITRAMAR), is now affiliated to the Federación de Asociaciones o Sindicatos Independientes de El Salvador (FEASIES). On January 15, the company's key customers committed to create a fund in exchange for finished product that was locked inside the factory; this fund was used to pay workers for their last week of work.

The January 15, 2014, agreement also stated that the equipment remaining inside the factory could be sold and the funds generated used toward the payment of 50% of the workers' severance and other terminal benefits. However, the factory had illegally closed operations without following proper legal procedures,[1] and owed money to government institutions and other creditors. Given this, the government seized control of the factory's assets.

The Argus Group violated Honduran law on several points. Most fundamentally, Argus failed to provide workers with legally owed severance pay. Article 58 of the Salvadoran Labor Code requires employers to provide any worker terminated in a no-fault dismissal with severance pay in the amount of one month of salary for each year of employment. The company's failure to do so violated the law and has created unnecessary hardship for workers who depend on legally-mandated severance that, in the absence of state-run unemployment insurance, serves as the only social safety net for workers during a period of unemployment. In addition, as noted above, Argus failed to follow the legal closure policies in closing down MDR/CCC, and failed to provide workers with their final week of pay. A separate section below will also detail violations of workers' associational rights committed by Argus during the period following the closure.

Response from Argus Group and MDR/CCC Buyers

Following the closure of the plant, worker representatives contacted the WRC to inform them of the closure and the associated violations. In response, the WRC made repeated attempts to contact the Argus Group, a Miami-based company that has operations in El Salvador and Nicaragua. Argus operates several factories including two in Nicaragua, Calypso and Kaltex Argus, a Nicaraguan facility that is a joint operation with the Kaltex Group of Mexico. The WRC had published a report on violations at multiple Argus Group factories in 2006.[2]

The two principles of Argus, Alfonso Hernandez and Roberto Bequillard, initially denied any relationship to or responsibility for MDR/CCC. However, the WRC found multiple

[1] Article 64 of the Salvadoran Code of Commerce states that a business that is going to dissolve its legal entity must take formal steps to do so thirty days prior to closure, publishing its intent to do so in El Salvador's Official Journal. According to the workers and the representatives, the company took no steps to formally petition closure; this was confirmed by the WRC's review of the Official Journal for the sixty days prior to its closure, http://www.diariooficial.gob.sv/diarios/do-2013/.

[2] "Case Summary: Calypso, Atlantic and Manufacturas del Rio (Nicaragua and El Salvador) ," December 19, 2006. Available at http://www.workersrights.org/Freports/Case%20Summary%20-%20Calypso,%20Atlantic%20and%20Manufacturas%20del%20Rio.pdf.

sources of documentary evidence in the public record confirming the names of the factory's legal representatives and the fact that the Argus Group operated both MDR and CCC.

On January 17, after investigating the facts of the closure, the WRC contacted firms sourcing from MDR/CCC. As a result, Hanesbrands and Fruit of the Loom pressed the Argus Group to comply with its obligations to the workers. In July 2014, the Argus Group made payments totaling US$650,000 towards the total amount owed to workers, approximately 37% of the total amount due. Argus Group affirmed that the remaining 63% of the total amount due would be generated by the sale of the goods.

The WRC did not feel that waiting for the sale of the goods was a viable solution. In the experience of the WRC and worker advocates in El Salvador, the process by which these goods are inventoried, appraised and auctioned for sale is a process that can take months or even years. This perspective has been borne out by the facts in this case; the MDR/CCC assets currently – one year and four months after the date of the factory's closure – have not yet been sold. These delays have been despite the fact that Hanesbrands and Fruit of the Loom, working with the unions representing the MDR/CCC workers and with the WRC, engaged in significant efforts to press the government to complete the auction of goods. At this time, the relevant government agency reports that it is still in the process of completing one of the necessary prerequisites, an inventory of goods.

The WRC communicated these reservations to the factory's buyers, and continued to emphasize the importance of promptly and completely making the workers whole, rather than waiting for an unpredictable process that was unlikely to move quickly or generate adequate sums to provide workers with all of the severance pay that they were owed.

In early 2015, Hanesbrands and Fruit of the Loom agreed to provide the sums necessary to make the workers whole. The Levi Strauss licensee Hampshire had committed by this point to make a small contribution as well, of US$30,000. Lacoste, which is owned by the Swiss firm Maus Freres, recognized that its intermediary in El Salvador was subcontracting work to MDR, but refused to provide any funds towards the unpaid severance. This is particularly notable given that Lacoste had a significant amount of production in the factory; other buyers report that Lacoste purchased approximately 30% of the factory's output during the period prior to closure. A Lacoste representative was initially involved in meetings on the ground following the factory closure, and the company may have contributed some money towards workers' final unpaid wages, in hopes of obtaining its finished goods from the factory, but the company's failure to take responsibility for ensuring that workers were made whole stands in unfavorable contrast to the positive actions taken by Hanesbrands and Fruit of the Loom.

Based on calculations provided by the two unions, and reviewed by the WRC, Hanesbrands and Fruit of the Loom agreed to provide a total of US$1.07 million. Along with the funds from Hampshire and funds that were unclaimed following the July 2014 distribution, this was sufficient to make all workers whole for the amount owed at the time of closure. Subsequent to this agreement, a small group of workers, who had been terminated prior to the factory closure and were owed a total of approximately US$9,000, presented their case to the two unions. The unions and brands agreed to divide the funds among these workers as well, meaning that each worker will receive approximately 99%, rather than 100%, of what they are owed.

Severance Pay Owed and Provided to MDR/CCC Workers	
Total Severance Due at Time of Closure	$ 1,760,318
Paid by Employer in July 2014	$ 650,000
Unclaimed Funds from First Distribution	$ 6,746
Contributed by Levi/Hampshire	$ 30,000
Contributed by Hanesbrands	$ 574,000
Contributed by Fruit of the Loom/Russell	$ 500,000
Principal Amount Still Owed to Workers	$ 0

The distribution of these funds began on April 27, 2015, and was ongoing at the time of this report. Checks made out to each worker are being made available first at the Ministry of Labor and then at a local bank for a total distribution time of one month. The sum to be paid to each worker was determined based on the terminal benefits as calculated by the Salvadoran Ministry of Labor at the time of the closure minus the amount that was paid to each worker in July 2014. The WRC is observing the distributions.

As noted above, this does not include interest, which is an important element in remedying any case in which workers are denied funds they are legally owed for an extended period of time. In this case, the WRC calculated the average commercial interest rate during the period that the workers were denied the funds they were owed, and it is quite high: 30.3%. (Most workers who have borrowed money have done it at even higher interest rates, as they cannot access bank loans and instead are forced to borrow from neighborhood lenders charging rates far above the commercial rates.) Using the commercial rate, workers are owed several hundred thousand dollars in interest.

Fortunately, while the timing remains uncertain, the WRC is confident that the process of liquidation of the factories assets will generate additional funds sufficient to pay workers a reasonable approximation of the interest accrued. For this reason, and in light of the sizable contributions the companies have made, the WRC considers the violations resolved with regard to Fruit of the Loom/Russell, the licensee that sourced university logo product from these facilities, and with regard to Hanesbrands, and we consider the university code violations at the factory to be remedied. The WRC will continue to monitor the liquidation process and will also continue to urge Lacoste to act responsibly and contribute toward the interest owed to the workers.

Freedom of Association

In the decade prior to the closure of MDR/CCC, workers formed two unions at the factory. In 2006, workers formed a factory-level union affiliated to the Sindicato de la Industria Textil (STIT) in 2006.[3] This union represented more than 400 MDR/CCC employees at the time of closure. In 2011, workers formed the SITRAMAR union, which is now affiliated to the Federación de Asociaciones o Sindicatos Independientes de El Salvador (FEASIES). SITRAMAR represented a significantly smaller number of workers. Workers report that both unions participated in a strike that took place in October 14-18, 2013.

Workers reported that they had initiated the strike because of concern that unilateral changes made by the company were endangering their benefits and seniority. These benefits, and others, are based on workers' years of service with an employer. Workers reported that they believed that the company was shifting them from being employees of one of the two legal entities (MDR and CCC) to the other, without any explanation as to the implications of this change in legal employer, or commitment to preserve their years of service. The WRC has not investigated these allegations.

Following the strike, on October 30, 2013, the two unions that represent workers at MDR/CCC met with the plant manager. The unions proposed that the company commit to negotiate a collective bargaining agreement with the union that represented the larger percentage of workers, the STIT. The workers who are leaders in the STIT union had been pressing management to engage in collective bargaining for over a year.

[3] For additional information regarding the formation of the STIT union and related freedom of association violations, see "Case Summary: Calypso, Atlantic and Manufacturas del Rio (Nicaragua and El Salvador) ," December 19, 2006. Available at http://www.workersrights.org/Freports/Case%20Summary%20-%20Calypso,%20Atlantic%20and%20Manufacturas%20del%20Rio.pdf.

At this meeting, the plant manager and the company's legal counsel, Mario Sanchez, agreed to negotiate a collective bargaining agreement with the STIT union.[4] On November 1, 2013, the union presented a formal request to the Ministry of Labor to begin negotiation with the company, in accordance with the process denoted by Salvadoran law. On November 23, the Ministry of Labor notified the company of the union's request, and asked the company to respond within fifteen working days as to whether or not it was also willing to enter into bargaining. The STIT union has informed us that they are not aware of any response to this communication.

On November 30, 2013, workers report, the plant manager informed the workers that his superiors at Argus had not agreed to participate in the bargaining process and that he was being transferred to one of the company's Nicaraguan facilities. Approximately one week later, a worker who is a union leader reports, the manager called this union leader to his office and told him that Argus was not interested in investing any more funds into the factory.

On January 7, 2014, workers returned from their end-of-year holiday to find the factory doors locked and no representative of management present. The security guards at the free trade zone distributed fliers with the following text:

> This note informs all of the employees of Manufacturas del Rio and CCC that effective Tuesday, January 7, 2014, the factory will discontinue operations for an indefinite period of time. This is in response specifically to the financial and operational damage to the company and its clients caused by an illegal strike organized in the month of October 2013 by workers who provide services to both companies. That same week, the courts declared the strike illegal. However, workers decided to continue with illegal actions and an operational boycott. While the company has made efforts to normalize production, it was impossible to overcome the damage, which has been accentuated by the uncertainty caused by continuous threats to repeat illegal actions during the rest of the year and 2014. Additionally, the delays caused by the strike resulted in non-fulfillment and important contracts were lost, which created an unsustainable economic situation for the company that has forced us to make this decision. We inform you that even though the responsibility for this unfortunate situation is inevitably linked to the aforementioned illegal actions, we urge the workers of the company to direct their consultations

[4] Salvadoran law allows employers to negotiate collective bargaining with unions whether or not they represent a majority of workers at a worksite. While the law states that the company will only be *obligated* to participate in bargaining when the union represents a majority of workers (Labor Code Article 270), the law does not prohibit the company from entering into negotiation with any legally-established union.

> to the corresponding entities. Any notification that should be made to the companies can be directed to this fax number: 2242-1891. This communiqué has been issued by the company's top management.[5]

The company claims that it was compelled to close the plant because of the "financial and operational damage to the company and its clients" caused by the October 2013 strike. It further states that "important contracts were lost." The WRC has reviewed the question of whether the closure was in fact a financial result of the strike, and has also considered the possibility that the factory was closed in response to workers' decision to press for a collective bargaining agreement.

However, the WRC has not found convincing evidence that the closure was either the financial result of the strike or a decision undertaken in retaliation for workers exercising their associational rights. Regarding the strike, it is worth noting that the strike itself substantially impacted factory production for only one week. In addition, key buyers assured the WRC in November and December 2014 that they were neither decreasing production nor planning to do so. Information provided by these buyers regarding MDR/CCC's financial stability in the months leading up to the closure leads the WRC to conclude that this closure was, in fact, the result of serious financial issues at the plant unrelated to the strike.

By falsely stating that the closure was due to the economic impact of workers' collective action, however, Argus Group violated workers' associational rights, which are protected by university codes of conduct as well as the International Labor Organization Conventions 87 and 98, which have been ratified by El Salvador. Such a statement sends a clear statement to all of the MDR/CCC workers, and other workers in the area, that engaging in collective action is likely to result in factory closures and massive job losses. This is particularly true because, had MDR/CCC negotiated a collective bargaining with the workers, it would have been the only collective bargaining agreement in the Salvadoran apparel sector.

Conclusion

This case represents an important step forward in the effort to ensure that workers at collegiate factories, when they are denied legally mandated compensation at the time of factory closure or mass dismissal, are, through the efforts of licensees, made whole for all monies legally owed – and that the university code violations are thereby remedied. Without any pressure from universities, students or other parties, the responsible licensee in this case, Fruit of the Loom/Russell, and another key buyer, Hanesbrands (which is the

[5] Translation by WRC.

parent of two university licensees, but was not producing university logo product at these facilities), stepped forward at the request of the WRC and took the steps necessary to ensure that the employees received the compensation they legally earned. Their efforts are appreciated and are, we believe, a sign of a growing recognition on the part of licensees that it is appropriate and necessary for them to take responsibility for correcting code violations involving denial of legally mandated compensation, even where direct payment to workers proves necessary.