

EFFECTIVE INCENTIVES: A PROPOSAL OF TWO CHANGES TO UNITED  
STATES FEDERAL LAW TO IMPROVE WORKING CONDITIONS IN OVERSEAS  
FACTORIES

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STATES FEDERAL LAW TO IMPROVE WORKING CONDITIONS IN OVERSEAS  
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## **Abstract**

Transnational corporations and their practice of outsourcing manufacturing jobs to less developed nations with less restrictive labor laws have created a system of production wrought with considerable labor abuse and which encourages zero accountability. For years, all relevant parties with the power to effect change - consumers, corporations, Western governments, international bodies - have refused to take the helm of the global social justice responsibility movement. In recent years, both corporations and consumers have made some effort to take responsibility for these serious labor abuses, but these endeavors have been unsuccessful at effecting genuine change in the treatment of factory labor. There has still not been a serious push by government entities - and especially not by the United States government, which has jurisdiction over many of the biggest corporations in the world - to implement policy changes effective at combating labor abuse. This paper will illustrate some of the labor abuses occurring in Chinese factory suppliers of major U.S. corporations, outline existing U.S. laws which can be modified to incentivize stakeholders to improve factory working conditions, and propose and defend two necessary policy changes: the introduction of a new tax credit, and the creation of the Alien Labor Statute, a law parallel to the Alien Tort Statute.

## **Chapter I: Introduction to Factory Worker Abuse**

Factory labor abuse is not a new practice. It happened for decades in the United States until laws were passed which prohibited certain practices and helped to curb some of the abuses. While labor abuse does still happen in America, it happens much less often than it once did.<sup>1</sup> The trend over the last several decades has been for transnational corporations to outsource manufacturing jobs to foreign nations where labor laws are less strict and production is cheaper. It has become more profitable to commission overseas factories which abuse their workers than to manufacture in a country with strictly enforced standards.<sup>2</sup> Nowhere is data more abundant on factory labor abuse than in China, which has been the center of attention of many non-governmental organizations (NGOs) and their investigations for years.

American corporations play a large role in the global and Chinese factory market, as well as being responsible for factories which do not provide their workers adequate living and working conditions. For example, Wal-Mart outsources the production of its products to almost 100,000 different factories around the world; tens of thousands of

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<sup>1</sup> "CLEAR Timeline of United States Labor History," *Center for Labor Education & Research*, University of Hawai'i - West O'ahu, <http://clear.uhwo.hawaii.edu/Timeline-US.html>.

<sup>2</sup> "Outsourcing: Where's Uncle Sam?" Bloomberg Businessweek, February 5, 2007, [http://www.businessweek.com/debateroom/archives/2007/02/outsourcing\\_wheres\\_uncle\\_sam.html](http://www.businessweek.com/debateroom/archives/2007/02/outsourcing_wheres_uncle_sam.html).

those factories are located in China.<sup>3</sup> In fact, Wal-Mart's own estimates indicate that if it were considered a sovereign nation, its \$18 billion spent on products from China in 2006 would have made it China's fifth largest export market.<sup>4</sup> Foxconn, the world's largest electronics manufacturer and Apple's biggest supplier, employs well over one million people in China.<sup>5</sup> Dollar General commissions around 1,000 factories in China alone.<sup>6</sup> The clothing and apparel market continues to be one of the largest import markets for the United States from China, and China's clothing and apparel exports to the United States in 2010 were estimated to be worth about \$38,470,006.<sup>7</sup>

The United States is by far the world's largest merchandise importer; because much of this merchandise is manufactured in factories, the United States is also the world's largest factory-made goods importer.<sup>8</sup> This is further evidenced by the data on Wal-Mart's imports from China and China's apparel exports to the United States. This is important because it indicates that if labor abuses can be remedied in factories which supply American corporations, then a large dent can be made in global labor abuse prevalence. This supports an American-led solution.

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<sup>3</sup> "Wal-Mart Standards Fail, Workers Suffer," *China Labor Watch*, p. 2, November 25, 2009, <http://www.chinalaborwatch.org/pdf/20091125.pdf>.

<sup>4</sup> "Wal-Mart Standards Fail, Workers Suffer," p. 2.

<sup>5</sup> "Workers as Machines: Military Management in Foxconn," *Students & Scholars Against Corporate Misbehaviour*, p. 1, October 10, 2010, [http://sacom.hk/wp-content/uploads/2010/11/report-on-foxconn-workers-as-machines\\_sacom.pdf](http://sacom.hk/wp-content/uploads/2010/11/report-on-foxconn-workers-as-machines_sacom.pdf).

<sup>6</sup> "An Investigation of Suppliers of Dollar General," *China Labor Watch*, p. 2, August 10, 2010, [http://www.chinalaborwatch.org/upfile/2010\\_11\\_3/20101131312392.pdf](http://www.chinalaborwatch.org/upfile/2010_11_3/20101131312392.pdf).

<sup>7</sup> "Investigation of Two Clothing and Apparel Factories in China," *China Labor Watch*, p. 4, November 29, 2011, <http://www.chinalaborwatch.org/pdf/20111129-final.pdf>.

<sup>8</sup> "International Trade Statistics 2011," *World Trade Organization*, p. 16, [http://www.wto.org/english/res\\_e/statis\\_e/its2011\\_e/its11\\_merch\\_trade\\_product\\_e.pdf](http://www.wto.org/english/res_e/statis_e/its2011_e/its11_merch_trade_product_e.pdf).



To avoid unfair generalizations of Chinese labor conditions, this paper analyzes a large data sample, including factories from multiple sectors of the economy, multiple factories in each of those sectors, and factories which supply multiple American corporations. The investigations studied for this paper include several markets: electronics, clothing and apparel, general fabric, hand tools, paper, packaging, plastics, and miscellaneous goods. The studies cover over 25 factories in China which supply many U.S. corporations, the biggest of which are Apple, Wal-Mart, Dollar General, Dell, IBM, Microsoft, Hewlett-Packard, and American Eagle.<sup>9,10,11,12</sup>

These studies employed reliable research methodology given the cultural and legal barriers investigators in China encounter. In nearly every cited investigation, at least 100 workers were interviewed, and in one study over 408 workers were consulted. In one investigation in which the number of factory workers interviewed was less than 100, the investigation focused on two factories with less than 300 workers. In an investigation in which the number of interviewed workers is unknown, investigators actually infiltrated the factory by posing as workers to verify claims made by workers in interviews. This undercover hiring also happened in two other studies. Due to the thoroughness of the investigations, the impartiality of the research methodologies, as well as the experience of

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<sup>9</sup> “Tragedies of Globalization: The Truth Behind Electronics Sweatshops,” p. 2.

<sup>10</sup> “Wal-Mart Standards Fail, Workers Suffer.”

<sup>11</sup> “An Investigation of Suppliers of Dollar General.”

<sup>12</sup> “Investigation of Two Clothing and Apparel Factories in China,” p. 4.

each organization which published these findings, these studies provide the best currently available data.<sup>13</sup>

The table below compares each investigative study's findings. The factories are grouped into relevant categories: ten different electronics factories have been grouped together; Foxconn was kept separate due to its size, but its category includes two different Foxconn factories; seven factories which supply Wal-Mart are one group, as are four factories which supply Dollar General, and two general apparel factories. Here is the table: <sup>14,15,16,17,18,19</sup>

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<sup>13</sup> China Labor Watch, which published five of the cited investigations, has been publishing investigations online since January of 2000; since then CLW has published dozens of investigations on labor abuse. Students and Scholars Against Corporate Misbehavior has been publishing investigations online since 2005, and similarly published dozens of investigations since.

<sup>14</sup> "Tragedies of Globalization: The Truth Behind Electronics Sweatshops," *China Labor Watch*, pp. 7-134, July 12, 2011, <http://chinalaborwatch.org/pdf/20110712.pdf>.

<sup>15</sup> "Workers as Machines: Military Management in Foxconn," pp. 6-24.

<sup>16</sup> "Wal-Mart Standards Fail, Workers Suffer," 3-21.

<sup>17</sup> "Wal-Mart's Road to Sustainability: Paved with False Promises?," *China Labor Watch*, pp. 3-27, July 27, 2009, [http://www.chinalaborwatch.org/investigations/2009\\_07\\_27/Walmart%20Report.pdf](http://www.chinalaborwatch.org/investigations/2009_07_27/Walmart%20Report.pdf).

<sup>18</sup> "An Investigation of Suppliers of Dollar General," pp. 3-13.

<sup>19</sup> "Investigation of Two Clothing and Apparel Factories in China," pp. 4-23.

<b>CRITERIA</b>	<b>ELECTRONICS SUPPLIERS</b>	<b>FOXCONN</b>	<b>WAL-MART</b>	<b>DOLLAR GENERAL</b>	<b>APPAREL FACTORIES</b>
Wages/Month	\$169 - \$227	\$190.11 - \$198.03	\$113 - \$265	-	-
Wages After Deductions	\$76	-	\$132	-	-
Overtime Wages	\$1.17/hr - \$2.35/hr	1.5 times normal wage	As little as \$0/hr	-	-
Wages Violate Labor Law	Yes	Yes and No	Yes	Yes	Yes
Wages Meet Living Costs	No	No	No	No	No
Work Hours	40/week	42/week - 60/week	40/week	-	40/week
Overtime Hours/ Month	20 - 160	36 - 140	40 - 140	100 - 300	120
Overtime Violates Labor Law	Very Often	Very Often	Yes	Yes	Yes
Work Intensity	Extremely High	Extremely High	Extremely High	Extremely High	Extremely High
Written Contracts	Not Always	Not Always	Not Always	No	No
Contracts Violate Labor Law	Often	Sometimes	Often	Yes	Yes
Discrimination	Yes	Yes	Yes	Yes	Yes
Number of Workers Per Dorm	-	10	~10	-	-
Other Poor Dorm Conditions	-	Yes	Yes	-	-
Safety Violations	Yes	Yes	Yes	Yes	Yes
Audit Falsification	Yes	Yes	Yes	Yes	Yes

This table summary suggests certain similarities and dissimilarities between these factories:

<b>SIMILARITIES</b>	
Wages Violate Labor Law	Yes
Wages Meet Living Costs	No
Overtime Violates Labor Law	At Least Very Often
Work Intensity	Extremely High
Contracts Violate Labor Law	At Least Sometimes
Discrimination	Yes
Safety Violations	Yes
Audit Falsification	Yes

Notably, all of the factories have similar patterns of abuse: labor law violations, sub-standard wages, discrimination, unsafe working conditions, audit falsification. Some factories have worse conditions than others, but none of the investigated factories meet the minimum legal requirements in every category. This data provides justification for creating legal mechanisms in the United States to fix these labor abuse issues: it is clearly common for factories to violate China's labor laws, and not much is being done to end the cycle of abuse. The factories falsify audits, so it is difficult for both the Chinese government and U.S. corporations to get accurate information on the living and working conditions in each factory. Legal changes can alleviate many of these problems, and the specifics will be discussed in Chapter III, but first, more specific insight into particular factory and worker conditions is needed.

To evaluate specific factory conditions, ten of the factories from the investigatory reports cited above were isolated. Reasons for their selection include the availability of data for each factory as well as variety in the products and services each factory provides. The first labor abuse issue surveyed in depth will be wages. When evaluating the

adequacy of a factory wage, it is important to compare it to two different measurements: the cost of living in the region in which the factory is located, and the legal minimum wage of that region. The cost of living is the cost of maintaining a certain standard of living, and in the context of this paper it is referring to the cost of maintaining a reasonable quality of life relative to the region - clothes, food, shelter, occasional entertainment, healthcare expenses, and unforeseeable family expenses. When workers' wages do not meet their cost of living, they do not necessarily die; rather, they are just unable to attain a reasonable quality of life. Due to the difficulty of measuring the "cost of living" in many of these regions and the relative unavailability of such data, per capita consumption expenditure will serve that purpose.<sup>20</sup>

Per capita consumption expenditure is the average measure of the market value of all goods and services purchased by a local resident.<sup>21</sup> Since the per capita consumption expenditure is the average consumption of every individual in a region, it includes the consumption levels of the relatively rich and that of the relatively poor. While it is difficult to say for certain the relationship between the cost of living and this consumption index, for the purposes of this thesis, it will be assumed that they are similar values. There is evidence to suggest that the true cost of living in many of these regions is actually significantly higher than the per capita consumption expenditure because the

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<sup>20</sup> According to SACOM, the formula for living wage derived from Engel's Law is (food expenditure ÷ percentage of income spent on food x dependency ratio). Measures for consumption expenditure very often come from regional governments themselves; while some do break down consumption expenditure by category (thereby making "food expenditure" a known value), not all local governments report the percentage of income spent on food, and very few local governments report the average dependency ratio of the region. The unavailability of these values makes a "living wage" or the "cost of living" all but impossible to calculate for all regions.

<sup>21</sup> *Investopedia*, "Personal Consumption Expenditures," accessed March 7, 2012, <http://www.investopedia.com/terms/p/pce.asp#axzz1oUTZIx8p>.

consumption expenditure is skewed by the fact that many in each region consume at levels well below the cost of living.<sup>22</sup> This evidence does not cover every relevant region, however, so it is best to use per capita consumption expenditure for the initial comparison. The following table shows consumption expenditure and wage data for six electronics factories, three Wal-Mart factories, and one Dollar General Factory:<sup>23,24,25,26,</sup>

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<b>FACTORY</b>	<b>REGION</b>	<b>CONSUMPTION EXPENDITURE</b>	<b>REGIONAL MINIMUM WAGE</b>	<b>CURRENT FACTORY MINIMUM WAGE</b>
Hongkai Electronics	Dongguan	\$248.83	\$174.27	\$169.40
Catcher Technology	Suzhou	\$277.39	\$180.61	\$175.56
Kunshan Compal	Kunshan	\$305.38	\$180.61	\$175.56
Flextronics	Zhuhai	\$203.38	\$174.27	\$202.51
Foxconn Kunshan	Kunshan	\$305.38	\$180.61	\$235.62
Foxconn Longhua	Shenzhen	\$242.70	\$173.89	\$184.80
Dashing Decoration	Dongguan	\$248.83	\$174.27	\$113
Stanley Tool	Zhongshan	-	\$174.27	\$115
Huasheng Packaging Factory	Huasheng	\$180.61	\$174.27	\$102.98
Yiu Yi Plastic & Mould	Shenzhen	\$242.70	\$173.89	\$129

<sup>22</sup> “Workers as Machines: Military Management in Foxconn,” p. 7.

<sup>23</sup> “Tragedies of Globalization: The Truth Behind Electronics Sweatshops,” pp. 126-133.

<sup>24</sup> “Workers as Machines: Military Management in Foxconn,” p. 7.

<sup>25</sup> “Wal-Mart Standards Fail, Workers Suffer,” 3-21.

<sup>26</sup> “Wal-Mart’s Road to Sustainability: Paved with False Promises?” pp. 3-27.

<sup>27</sup> “An Investigation of Suppliers of Dollar General,” pp. 3-13.

The information in this table clarifies two points. First, for all regions for which there are per capita consumption expenditure data, the legal minimum wage is below consumption expenditure. This is especially important, because it indicates that even if factories were following the regional labor laws and paying their workers the legal minimum wage, those wages are still not fair to the workers, because the wages do not provide a reasonable standard of living. In the status quo, though, this is a moot point, because the second clear fact is that all of the factories except Flextronics and the two Foxconn locations do not even pay their workers legal wages. Some factories pay workers far below the legal minimum; at Dashing Decoration, the legal minimum wage is actually 65% higher than the factory minimum wage. What exists here is a legal minimum wage that is higher than the wages being paid and yet still lower than a reasonable wage. Workers should to be paid enough to maintain a reasonable standard of living; doing so is an economically viable option. With the proper incentives, corporations can afford to increase wages at these factories, as will be proven in Chapter III.

Another major area of labor abuse is that of overtime hours and wages. According to China's Labor Law, workers cannot work more than 40 hours per week without receiving overtime compensation. Additionally, a factory cannot require more than one hour of overtime per day (with the rare exception of three hours per day in special circumstances), and no more than 36 hours per month.<sup>28</sup> The following table, borrowed

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<sup>28</sup> Labor Law of the People's Republic of China, July 5, 1994, Order Number 28, Eighth National People's Congress, <http://www.usmra.com/china/Labour%20Law.htm>.

from Nathan Jackson at The University of Iowa Center for International Finance and Development, shows the rules governing overtime pay in China's Labor Law:<sup>29</sup>

<b>Extended Working Hours</b>	<b>Minimum Overtime Pay (percent of regular wages)</b>
Typical working day	150 percent
Rest day (min. one per week) (i.e., weekend)	200 percent
National holiday	300 percent

Based on this scale, workers should be getting paid a minimum of 150% of their regular wages for a maximum of 36 hours of overtime per month. None of the ten selected factories strictly follows this regulation: <sup>30, 31, 32, 33, 34</sup>

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<sup>29</sup> Nathan Jackson, "What Are the Major Aspects of Chinese Labor Law," *The University of Iowa Center for International Finance and Development*, April 2011, accessed March 3, 2012, <http://blogs.law.uiowa.edu/ebook/uicifd-ebook/what-are-relevant-issues-concerning-chinese-labor-and-employment-law>.

<sup>30</sup> "Tragedies of Globalization: The Truth Behind Electronics Sweatshops," pp. 7-134.

<sup>31</sup> "Workers as Machines: Military Management in Foxconn," pp. 7-8.

<sup>32</sup> "Wal-Mart Standards Fail, Workers Suffer," pp. 3-21.

<sup>33</sup> "Wal-Mart's Road to Sustainability: Paved with False Promises?" pp. 3-27.

<sup>34</sup> "An Investigation of Suppliers of Dollar General," pp. 3-13.



<b>FACTORY</b>	<b>AVERAGE OVERTIME HOURS</b>	<b>AMOUNT OVER FEDERAL LIMIT</b>	<b>FACTORY OVERTIME WAGE</b>	<b>OVERTIME WAGE VIOLATES LABOR LAW</b>
Hongkai Electronics	60 - 120	24 - 84	-	Yes
Catcher Technology	75	39	-	Yes
Kunshan Compal	40	4	\$1.18/hr	Yes
Flextronics	20 - 130	0 - 94	-	Yes
Foxconn Kunshan	45	9	-	No
Foxconn Longhua	40	4	-	No
Dashing Decoration	80	44	\$.44/hr	Yes
Stanley Tool	40	4	-	Yes
Huasheng Packaging Factory	70	34	\$.71/hr	Yes
Yiu Yi Plastic & Mould	100 - 300	64 - 264	\$1.11/hr	Yes

Only one factory - Flextronics - has an extended period of down time during which workers do not work more than the federal limit of 36 overtime hours, but this starkly contrasts with Flextronic's high time, which is accompanied by an average of 130 hours of overtime. Four of the factories - Kunshan Compal, Foxconn Kunshan, Foxconn Longhua, and Stanley Tool - have average overtime hours that do not greatly exceed the federal limit, indicating that there are likely short periods of compliance averaged with periods of noncompliance. The other five factories have average overtime hours that so exceed the federal limit that it is unlikely that they ever comply with the regulation. At Yiu Yi Plastic & Mould, laborers can work up to 300 hours of overtime per month. That

is an average of 10 hours of overtime per day. Combined with the eight regular hours of work, that is an 18-hour workday.

Another problem is that only the two Foxconn factories comply with the federal minimum wage for overtime wages. At the two Foxconn locations, workers are paid 150% of their regular wages, which are also in compliance with the regional minimum wage. At all other factories - even Flextronics, which also complies with its regional minimum wage - overtime is either underpaid as a percentage of regular wages (i.e. less than 150%), or too low due to the regular minimum wages being below legal standards.

Legal limits on the number of overtime wages are in place for the workers' safety and comfort. Working too many hours can cause dangerous levels of fatigue. Factory conditions, even when compliant with safety regulations, are relatively dangerous, and high numbers of overtime hours further expose workers to danger.<sup>35,36,37,38</sup> Examples of these safety risks abound: in electronics factories, there is a high risk of contraction of occupational illnesses;<sup>39</sup> Stanley Tool, while providing workers with masks and earplugs, deny workers safety gloves;<sup>40</sup> workers in both Stanley Tool and Wing Fat Box Company complain of intense heat within the factory;<sup>41</sup> at Dollar General supply factories, raw

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<sup>35</sup> "Tragedies of Globalization: The Truth Behind Electronics Sweatshops," pp. 7-134.

<sup>36</sup> "Workers as Machines: Military Management in Foxconn," pp. 15-16.

<sup>37</sup> "Wal-Mart Standards Fail, Workers Suffer," pp. 3-21.

<sup>38</sup> "An Investigation of Suppliers of Dollar General," pp. 3-6.

<sup>39</sup> "Tragedies of Globalization: The Truth Behind Electronics Sweatshops," p. 99.

<sup>40</sup> "Wal-Mart Standards Fail, Workers Suffer," p. 15.

<sup>41</sup> "Wal-Mart Standards Fail, Workers Suffer," pp. 16, 19.

materials are piled haphazardly and chemicals are handled improperly, increasing the risk of harm to workers.<sup>42</sup>

Long workdays and significant overtime hours also detract from workers' quality of life, because they have no spare time for entertainment or family, which the Chinese traditionally hold to be important.<sup>43</sup> It is imperative that workers not be required to work more than 36 hours of overtime per month. Working more than 36 overtime hours per month ought to be presented as an option to workers who need the money, just as working long days with abundant overtime is an option for many Americans. Factories should not, however, be allowed to *require* abusive amounts of overtime of their workers, and in that regard China's Labor Law would be sufficient in preventing abuse if properly enforced.

The legal minimum overtime wage also has logical reasons for existence. As a laborer works more hours per day, each hour becomes more valuable to him. This is because with each hour that a worker spends in the factory, he has one fewer hour to allocate to another activity. There are also the issues of fatigue and increased exposure to dangerous equipment and conditions. After a certain number of hours of work (the law says 40 per week), the laborer's time becomes financially worth 50% more than the first 40 hours. This logic is further supported by the law's requirements for rest day and holiday overtime wages: the time on those days is considered substantially more valuable than the regular 40 work hours, so the work gets rewarded with double and triple wage

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<sup>42</sup> "An Investigation of Suppliers of Dollar General," p. 3.

<sup>43</sup> "The Traditional Chinese Family & Lineage," David K. Jordan, University of California San Diego, accessed April 20, 2012, <http://weber.ucsd.edu/~dkjordan/chin/hbfamilism-u.html>.

rates, respectively. Current Chinese labor law underscores that a worker's time has a scalable financial value, but most of the studied factories do not respect this.

Available data paints a clear picture of labor abuse in Chinese factories which supply American corporations. The abuses defy Chinese regulations, though China's labor standards are already insufficient. Watchdog groups continue to investigate and shed light on labor abuses, but the illegal and unethical practices continue. This paper proposes two U.S. legal mechanisms as viable and constitutional pathways to ending labor abuse abroad.

## **Chapter II: Introduction to Existing Law**

Now that it has been established that there is a labor abuse problem, it is necessary to review the current laws and infrastructure that might be adapted for the purpose of ending the abuse. The first step is to guarantee that an attempt to fix foreign labor abuse is permitted by the United States Constitution. Second, this paper considers three relevant sections of the United States Code, which is the compilation of federal laws passed by Congress: one that covers tax credits, one that grants jurisdiction to U.S. federal courts in cases filed by non-citizens, and one that discusses the main trade negotiating objectives of the United States. The last objective of this chapter is to discuss existing trade agreements with foreign countries and how those might be altered to prevent trade and political backlash from economic partners.

### **Part One: The United States Constitution**

Article One, Section Eight of the United States Constitution enumerates the powers of Congress. Section Eight provides the legal foundation for attempting to curb labor abuses in foreign countries: “The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises, [...] To regulate Commerce with foreign Nations,

and among the several States, and with the Indian Tribes.”<sup>44</sup> In these two sentences alone one finds all of the required Constitutional justification for such a plan; Congress can impose taxes, regulate imports, and dictate how American businesses trade with foreign nations.

These powers have been further affirmed through a plethora of federal court decisions. In the *License Tax Cases*, a Supreme Court Decision on a group of seven similar cases, the Court wrote that “That the recognition by the acts of Congress of the power and right of the States to tax, control, or regulate any business carried on within its limits, is entirely consistent with an intention on the part of Congress to tax such business for National purposes.”<sup>45</sup> This decision effectively expanded Congress’ taxation power so that it included the ability to tax business as a regulation as opposed to simply to raise national funds. A later case, *McCray v. United States*, expanded this power even further by giving Congress the ability to tax a business with the intention of eliminating that business, writing that “the manufacture of artificially colored oleomargarine may be prohibited by a free government without a violation of fundamental rights.”<sup>46</sup>

The Supreme Court affirmed Congress’ power of import regulation and tariffs in *J.W. Hampton, Jr. & Co. v. United States*, concluding that “So long as the motive of Congress and the effect of its legislative action are to secure revenue for the benefit of the general government, the existence of other motives [such as to discourage particular

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<sup>44</sup> The United States Constitution, adopted by the Constitutional Convention, September 17, 1787, accessed on March 14, 2012, [http://www.archives.gov/exhibits/charters/constitution\\_transcript.html](http://www.archives.gov/exhibits/charters/constitution_transcript.html).

<sup>45</sup> *License Tax Cases*, The United States Supreme Court, 72 U.S. 462 (1866), p. 462, <http://caselaw.lp.findlaw.com/cgi-bin/getcase.pl?court=us&vol=72&invol=a>.

<sup>46</sup> *McCray v. United States*, The United States Supreme Court, 195 U.S. 27 (1904), p. 64, <http://supreme.justia.com/cases/federal/us/195/27/case.html>.

actions or the existence of particular industries] in the selection of the subjects of taxes cannot invalidate congressional action.”<sup>47</sup>

Justice Stevens, in his *Gonzales v. Raich* decision, wrote of the importance of the U.S. Constitution’s Commerce Clause,

In assessing the validity of congressional regulation, none of our Commerce Clause cases can be viewed in isolation. As charted in considerable detail in *United States v. Lopez*, our understanding of the reach of the Commerce Clause, as well as Congress' assertion of authority thereunder has evolved over time. The Commerce Clause emerged as the Framers' response to the central problem giving rise to the Constitution itself: the absence of any federal commerce power under the Articles of Confederation. For the first century of our history, the primary use of the Clause was to preclude the kind of discriminatory state legislation that had once been permissible. Then, in response to rapid industrial development and an increasingly interdependent national economy, Congress "ushered in a new era of federal regulation under the commerce power," beginning with the enactment of the Interstate Commerce Act in 1887, and the Sherman Antitrust Act in 1890.<sup>48</sup>

Justice Stephens goes on to enumerate “three general categories of regulation” which federal cases have granted Congress: “First, Congress can regulate the channels of interstate commerce. Second, Congress has authority to regulate and protect the instrumentalities of interstate commerce, and persons or things in interstate commerce. Third, Congress has the power to regulate activities that substantially affect interstate commerce.”<sup>49</sup> All of this illustrates that the United States Federal Government has well-established authority to collect taxes, police imports, and regulate interstate commerce

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<sup>47</sup> *J.W. Hampton, Jr. & Co. v. United States*, The United States Supreme Court, 276 U.S. 394 (1928), p. 412, <http://supreme.justia.com/cases/federal/us/276/394/case.html>.

<sup>48</sup> *Gonzales v. Raich*, The United States Supreme Court, 545 U.S. 1 (2005), p. 12, [http://scholar.google.com/scholar\\_case?case=15647611274064109718](http://scholar.google.com/scholar_case?case=15647611274064109718).

<sup>49</sup> *Gonzales v. Raich*, p. 13.

and commerce with foreign nations. It will be argued later that only the power to lay and collect taxes is necessary for the enactment of a legal mechanism which will mitigate much foreign labor abuse.

Controlling imports is not a reasonable or practical approach to the labor abuse problem, though. First, the import of factory-made goods is a profitable and common economic endeavor.<sup>50</sup> This has two major impacts on the situation: the first is that enforcement becomes nearly impossible. The U.S. Customs office does not have the resources necessary to screen all factory-made goods to guarantee that they are all made in factories which satisfy their labor laws. Even if the Customs office did have the resources to do so, the economic impact of such a policy would be tremendous. Many corporations would have to pay substantial amounts of money to guarantee compliance; those that could not guarantee compliance would have their products seized upon entry in the United States. The Customs office would be spending untold amounts of money to monitor factories all around the world. Such a scenario is simply not tenable from either an economic standpoint or an enforcement standpoint. Finally, the power to regulate commerce with foreign nations is important in this calculation, but it ends up being an indirect requirement. Since most corporations do not actually own the overseas factories, importation is required to move products from the factories to the stores within the United States. Without the power to regulate commerce with foreign countries, the government would have no say in how corporations do business with their overseas factories, and it would be impossible for regulation to occur.

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<sup>50</sup> "International Trade Statistics 2011," *World Trade Organization*, [http://www.wto.org/english/res\\_e/statis\\_e/its2011\\_e/its11\\_merch\\_trade\\_product\\_e.pdf](http://www.wto.org/english/res_e/statis_e/its2011_e/its11_merch_trade_product_e.pdf).



Another important section of the Constitution is Article Three, which establishes the Supreme Court of the United States and creates the legal foundation for the federal judiciary system.<sup>51</sup> The second half of this paper's proposed two-pronged legal solution to labor abuse deals exclusively with the federal judiciary and its jurisdiction. What is important is that there is no constitutional barrier to Congress creating legislation that provides incentives to end foreign labor abuse.

## **Part Two: The United States Code Service**

There are three pertinent sections in the U.S. Code. The first is Title 26 "Internal Revenue Code," Subtitle A "Income Taxes," which covers the taxes that can be levied against an individual or corporation and the tax credits that can be given.<sup>52</sup> For example, Subpart D -- Business Related Credits contains over 20 tax credits for businesses that meet certain qualifications. Section 40 grants businesses a tax credit of "60 cents for each gallon of alcohol used by the taxpayer in the production of a qualified mixture."<sup>53</sup> The section goes on to outline what qualifies as an alcohol mixture fuel in significant detail. Section 45F grants businesses that provide employees with child care a tax credit of "25 percent of the qualified child care expenditures, and 10 percent of the qualified child care resource and referral expenditures."<sup>54</sup> This section also goes on to outline what kind of

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<sup>51</sup> The United States Constitution.

<sup>52</sup> Title 26 "Internal Revenue Code," Subtitle A "Income Taxes," 26 U.S.C. § 1 - 1564, accessed March 17, 2012, <http://www.gpo.gov/fdsys/pkg/USCODE-2010-title26/pdf/USCODE-2010-title26-subtitleA.pdf>.

<sup>53</sup> Alcohol used as fuel, 26 U.S.C. § 40, accessed March 14, 2012, [http://frwebgate.access.gpo.gov/cgi-bin/usc.cgi?ACTION=RETRIEVE&FILE=\\$xa\\$busc26.wais&start=999290&SIZE=31584&TYPE=PDF](http://frwebgate.access.gpo.gov/cgi-bin/usc.cgi?ACTION=RETRIEVE&FILE=$xa$busc26.wais&start=999290&SIZE=31584&TYPE=PDF).

<sup>54</sup> Employer-provided child care credit, 26 U.S.C. § 45F, accessed March 14, 2012, [http://frwebgate.access.gpo.gov/cgi-bin/usc.cgi?ACTION=RETRIEVE&FILE=\\$xa\\$busc26.wais&start=1464196&SIZE=12326&TYPE=PDF](http://frwebgate.access.gpo.gov/cgi-bin/usc.cgi?ACTION=RETRIEVE&FILE=$xa$busc26.wais&start=1464196&SIZE=12326&TYPE=PDF).

child care qualifies for the tax credit. Section 45A provides a similar tax credit to businesses which employ Indians.<sup>55</sup>

There are nearly two dozen of these kinds of tax credits, which outline how much the credit is worth and the proper conditions under which a business can qualify for the credit. Every credit could be considered a tax credit for making an ethical business decision: there are credits for aiding disabled individuals, using many kinds of alternative fuels, exploring new markets, maintaining railroad tracks, clinically testing drugs for rare diseases, and training mine rescue teams, just to name a few.<sup>56</sup> The existence of so many thoroughly outlined tax credits lends feasibility to the claim that a new tax credit should be introduced for businesses which guarantee a certain standard of work for the laborers in overseas factories. Considering how often similar credits have been introduced , it would not be unworkable to write and introduce such a tax credit.

An important feature of these tax credits is that they already have a well-developed bureaucratic infrastructure in the form of the Internal Revenue Service (IRS). The division most likely to cover businesses which commission overseas factories would be the Large Business and International Division (LB&I), one of the four major operating branches of the IRS. The LB&I Division serves corporations, subchapter S corporations, and partnerships with assets greater than \$10 million, and have a number of strategic

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<sup>55</sup> Indian employment credit, 26 U.S.C. § 45A, accessed March 14, 2012, [http://frwebgate.access.gpo.gov/cgi-bin/usc.cgi?ACTION=RETRIEVE&FILE=\\$\\$xa\\$busc26.wais&start=1396226&SIZE=14170&TYPE=PDF](http://frwebgate.access.gpo.gov/cgi-bin/usc.cgi?ACTION=RETRIEVE&FILE=$$xa$busc26.wais&start=1396226&SIZE=14170&TYPE=PDF).

<sup>56</sup> See 26 U.S.C. § 44, 26 U.S.C. § 40A, 26 U.S.C. § 43, 26 U.S.C. § 45, 26 U.S.C. § 45C, 26 U.S.C. § 45D, 26 U.S.C. § 45G, 26 U.S.C. § 45H, 26 U.S.C. § 45J, 26 U.S.C. § 45K, 26 U.S.C. § 45L, 26 U.S.C. § 45M, 26 U.S.C. § 45N

initiatives.<sup>57</sup> Some of the more relevant initiatives include the mission to “identify and address LB&I compliance risks for the increasingly global LB&I taxpayer,” the plan to “re-engineer and institutionalize issue management strategies and compliance processes,” and the method of using “partnerships, processes and legislative changes to provide timely data to effectively assess the reporting compliance risks in the LB&I population.”<sup>58</sup> With over 40 directors in the various branches and dozens of employees in the organizational structure<sup>59</sup> and an IRS Enforcement budget of nearly \$5.3 million,<sup>60</sup> this division with its strategic initiatives is well-organized and well-equipped to aid in the implementation and enforcement of a new tax credit which would provide improved standards for factory worker treatment.

A second relevant federal law is the Alien Tort Statute, which states that, “The district courts shall have original jurisdiction of any civil action by an alien for a tort only, committed in violation of the law of nations or a treaty of the United States.”<sup>61</sup> Included as part of the Judiciary Act of 1789, the ATS gives U.S. federal courts jurisdiction over cases filed by non-citizens which assert that a tortious violation of

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<sup>57</sup> “Large Business and International Division At-a-Glance,” *The Internal Revenue Service*, Last updated on January 23, 2012, accessed March 14, 2012, <http://www.irs.gov/irs/article/0,,id=96387,00.html>.

<sup>58</sup> “Large Business and International Division At-a-Glance.”

<sup>59</sup> “Large Business and International (LB&I) Division Directory,” *The Internal Revenue Service*, Last updated on March 13, 2012, <http://www.irs.gov/businesses/article/0,,id=134521,00.html>.

<sup>60</sup> “Budget Hearing - Office of Treasury IG and Office of Treasury IG for Tax Administration,” *Hearing Before the Committee on Appropriations Subcommittee on Financial Services and General Government, U.S. House of Representatives*, March 7, 2012, p. 2, accessed March 17, 2012, <http://appropriations.house.gov/UploadedFiles/HHRG-112-AP23-WState-JRussellGeorge-20120307.pdf>.

<sup>61</sup> Alien’s Action for Tort, 28 U.S.C. § 1350, accessed March 8, 2012, [http://frwebgate.access.gpo.gov/cgi-bin/usc.cgi?ACTION=RETRIEVE&FILE=\\$\\$xa\\$\\$busc28.wais&start=2639306&SIZE=4129&TYPE=PDF](http://frwebgate.access.gpo.gov/cgi-bin/usc.cgi?ACTION=RETRIEVE&FILE=$$xa$$busc28.wais&start=2639306&SIZE=4129&TYPE=PDF).

international law or U.S. treaties occurred.<sup>62</sup> While the history of this law is relatively short, it is complex. It is important to understand how the ATS developed before analyzing its impact on factory labor abuse.

Between 1789 and 1980, very few aliens invoked the ATS, and U.S. court jurisdiction was sustained through ATS only twice.<sup>63</sup> Moreover, there was little controversy over the statute's interpretation or application in any of the cases in which it was invoked.<sup>64</sup> In 1980, a single case changed all of that. *Filártiga v. Peña-Irala* was filed after the relatives of a young Paraguayan man found his torturer and murderer - also Paraguayan - living in New York City.<sup>65</sup> The family filed suit claiming that U.S. courts had jurisdiction under the ATS, because torture is considered a "tort ... in violation of the law of nations."<sup>66</sup> President Jimmy Carter filed a joint brief by the departments of State and Justice that strongly supported this view.<sup>67</sup> The district court dismissed the *Filártiga*' case due to a lack of subject matter jurisdiction, but the Second Circuit Court of Appeals overturned this view, instead recognizing that a universal consensus was emerging that international law guarantees certain rights to individuals, even from a State's treatment of

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<sup>62</sup> The Judiciary Act of 1789, Chapter 20, 1 Statute 73, 1st Congress, accessed March 8, 2012, [http://www.constitution.org/uslaw/judiciary\\_1789.htm](http://www.constitution.org/uslaw/judiciary_1789.htm).

<sup>63</sup> Jennifer K. Elsea, "The Alien Tort Statute: Legislative History and Executive Branch Views," *CRS Report for Congress*, October 2, 2003, p. 11, <http://www.policyarchive.org/handle/10207/bitstreams/1864.pdf>.

<sup>64</sup> Elsea, "The Alien Tort Statute: Legislative History and Executive Branch Views," p. 11.

<sup>65</sup> Beth Stephens, "Judicial Deference and the Unreasonable Views of the Bush Administration," *Brooklyn Journal of International Law*, 33 Brook. J. Int'l L. 773 (2008), p. 776, accessed March 9, 2012, [http://www.brooklaw.edu/~media/PDF/LawJournals/BJI\\_PDF/bji\\_vol33iii.ashx](http://www.brooklaw.edu/~media/PDF/LawJournals/BJI_PDF/bji_vol33iii.ashx).

<sup>66</sup> Stephens, "Judicial Deference and the Unreasonable Views of the Bush Administration," p. 776.

<sup>67</sup> Stephens, "Judicial Deference and the Unreasonable Views of the Bush Administration," p. 776.

its own citizens.<sup>68</sup> What is so interesting and significant about the decision in this case is not just that it revived the long-forgotten legal doctrine of the Alien Tort Statute, but also that it combined several different legal doctrines. It utilized the notion that liability for torts can follow the tortfeasor across international boundaries, a doctrine known as a transitory tort. The decision also argued that “federal courts should interpret international law as it has evolved and exists at the time of the case.”<sup>69</sup> Finally, the Second Circuit held that “deliberate torture perpetrated under the color of official authority violates universally accepted norms of the international law of human rights” and, thus, gave U.S. federal courts jurisdiction under the Alien Tort Statute.<sup>70</sup>

Since *Filártiga*, about 185 human rights cases have been filed, although the majority have been dismissed.<sup>71</sup> The most common reason for dismissal is a failure to prove that there was a violation of an actionable international norm.<sup>72</sup> While this case illustrates the origin of modern ATS common law, there is another landmark case in which the U.S. Supreme Court issued its first opinion on the ATS: *Sosa v. Alvarez-Machain*. *Sosa* was filed by Humberto Alvarez-Machain, a Mexican citizen who was kidnapped and brought to the United States to face trial for complicity in the murder of a Drug Enforcement Agency officer.<sup>73</sup> The DEA commissioned several Mexican nationals

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<sup>68</sup> Elsea, “The Alien Tort Statute: Legislative History and Executive Branch Views,” p. 13.

<sup>69</sup> Elsea, “The Alien Tort Statute: Legislative History and Executive Branch Views,” p. 13.

<sup>70</sup> Elsea, “The Alien Tort Statute: Legislative History and Executive Branch Views,” p. 13.

<sup>71</sup> Stephens, “Judicial Deference and the Unreasonable Views of the Bush Administration,” p. 776.

<sup>72</sup> Stephens, “Judicial Deference and the Unreasonable Views of the Bush Administration,” p. 777.

<sup>73</sup> Lucien Dhooge, “A Modest Proposal to Amend the Alien Tort Statute to Provide Guidance to Transnational Corporations,” *The UC Davis Journal of International Law & Policy*, 13 U.C. Davis J. Int'l L. & Pol'y 119, 134 (2007), p. 125, accessed March 14, 2012, [http://jilp.law.ucdavis.edu/issues/Volume%202013.2/Dhooge\\_5\\_15\\_07.pdf](http://jilp.law.ucdavis.edu/issues/Volume%202013.2/Dhooge_5_15_07.pdf).

unaffiliated with either the U.S. government or the Mexican government to kidnap Alvarez-Machain from his office and bring him to El Paso, Texas.<sup>74</sup> After hearing the government's case, the district court judge acquitted Alvarez-Machain on the grounds of insufficient evidence to support a guilty verdict.<sup>75</sup>

In 1993, Alvarez-Machain filed a lawsuit in the United States that named Sosa, six other Mexican nationals, the United States and four DEA agents as defendants. The lawsuit claimed that there were numerous constitutional and tort violations through the course of Alvarez-Machain's abduction, detention, and trial.<sup>76</sup> The district court ruled in favor of Alvarez-Machain's claim that transborder abductions are prohibited by international law norms which are "sufficiently established and articulated to support a cause of action under the [ATS]."<sup>77</sup> Upon appeal, the U.S. Court of Appeals for the Ninth Circuit upheld the district court's decision.

The Supreme Court granted certiorari on December 1, 2003. Justice Souter wrote the opinion, in which the Court unanimously agreed that Alvarez-Machain could not seek an ATS remedy.<sup>78</sup> Souter and the Court concluded that the ATS was intended to grant U.S. courts jurisdiction in a limited set of violations, namely the violation of safe conduct,

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<sup>74</sup> Dhooge, "A Modest Proposal to Amend the Alien Tort Statute to Provide Guidance to Transnational Corporations," p. 125.

<sup>75</sup> Dhooge, "A Modest Proposal to Amend the Alien Tort Statute to Provide Guidance to Transnational Corporations," p. 125.

<sup>76</sup> Dhooge, "A Modest Proposal to Amend the Alien Tort Statute to Provide Guidance to Transnational Corporations," p. 125.

<sup>77</sup> Dhooge, "A Modest Proposal to Amend the Alien Tort Statute to Provide Guidance to Transnational Corporations," p. 126.

<sup>78</sup> Dhooge, "A Modest Proposal to Amend the Alien Tort Statute to Provide Guidance to Transnational Corporations," p. 126-127.

infringement of rights of ambassadors, and piracy.<sup>79</sup> Furthermore, the Court put forth that claims over international law norms pursuant to the ATS were not recognizable if they had “less definite content and acceptance among civilized nations than the historical paradigms familiar when [the ATS] was enacted.”<sup>80</sup> The Court went on to conclude that Alvarez-Machain’s claim of transnational abduction is not one of these actions with recognizable international norms and thus not actionable under the ATS.<sup>81</sup>

The previous two cases establish the legislative history of the ATS. The most pertinent cases to the discussion in this thesis involve corporate liability. *Doe v. Unocal* is the decision that introduced the notion of corporate liability, and it has been upheld by many subsequent cases. In *Unocal*, the plaintiffs, Burmese Villagers, had suffered many human rights abuses at the hands of the Burmese military, including torture, rape, executions, and forced labor.<sup>82</sup> The villagers alleged that Unocal hired the Burmese military to provide security, despite knowing that the military would commit such human rights abuses.<sup>83</sup> Unocal filed a motion to dismiss on the grounds that corporations cannot be held liable under the ATS, but the district court denied this motion.<sup>84</sup> The district court went on to deny that it had jurisdiction on the grounds that the plaintiffs had failed to state a claim, because they “had not shown that Unocal controlled the Burmese military’s

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<sup>79</sup> Dhooze, “A Modest Proposal to Amend the Alien Tort Statute to Provide Guidance to Transnational Corporations,” p. 127.

<sup>80</sup> Dhooze, “A Modest Proposal to Amend the Alien Tort Statute to Provide Guidance to Transnational Corporations,” p. 130.

<sup>81</sup> Dhooze, “A Modest Proposal to Amend the Alien Tort Statute to Provide Guidance to Transnational Corporations,” p. 131-132.

<sup>82</sup> Stephens, “Judicial Deference and the Unreasonable Views of the Bush Administration,” p. 778-779.

<sup>83</sup> Stephens, “Judicial Deference and the Unreasonable Views of the Bush Administration,” p. 779.

<sup>84</sup> Stephens, “Judicial Deference and the Unreasonable Views of the Bush Administration,” p. 779.

actions, a necessary element in order to establish Unocal's liability."<sup>85</sup> The Ninth Circuit of Appeals reversed this decision, holding that it was sufficient to prove that Unocal aided and abetted a human rights violation by providing "knowing practical assistance or encouragement which has a substantial effect on the perpetration of the crime" in order to ascribe liability to Unocal.<sup>86</sup>

This decision opened a floodgate of legal cases; approximately 50 ATS cases have been filed against corporations since.<sup>87</sup> Courts have consistently held in many of these cases that corporations can be held liable for human rights abuses under the ATS, although some have been dismissed on other grounds.<sup>88</sup>

The final relevant piece of federal code is contained within the larger section of "Overall and Principal Trade Negotiating Objectives of the United States":

**(14) Worker rights**

The principal negotiating objectives of the United States regarding worker rights are—

- (A) to promote respect for worker rights;
- (B) to secure a review of the relationship of worker rights to GATT articles, objectives, and related instruments with a view to ensuring that the benefits of the trading system are available to all workers; and
- (C) to adopt, as a principle of the GATT, that the denial of worker rights should not be a means for a country or its industries to gain competitive advantage in international

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<sup>85</sup> Elsea, "The Alien Tort Statute: Legislative History and Executive Branch Views," p. 21.

<sup>86</sup> Stephens, "Judicial Deference and the Unreasonable Views of the Bush Administration," p. 779.

<sup>87</sup> Stephens, "Judicial Deference and the Unreasonable Views of the Bush Administration," p. 773.

<sup>88</sup> Stephens, "Judicial Deference and the Unreasonable Views of the Bush Administration," p. 779.



trade.<sup>89</sup>

This is a stated goal of the United States when negotiating trade agreements. Note that this single section contains all of the support necessary for enacting legal mechanisms to mitigate factory labor abuse: the United States wants to promote workers rights, it wants the benefits of the trading system to be available to all workers, and it does not want countries or industries to use the denial of worker rights as a means to gain competitive advantage in international trade. Given that these are goals that the United States intends to accomplish through its trade and trade negotiations, there are few legal barriers to accomplishing moderate goals in the realm of factory labor abuse.

### **Part Three: Trade Agreements**

It is worth analyzing existing trade agreements to determine if there are any barriers to the United States interfering with foreign countries' internal business affairs. In the instance of China, the trade agreement to focus on would be the World Trade Organization's *Report of the Working Party on the Accession of China*. Chapter III focuses on the policy enforcement system. China's representative to the WTO stated on more than one occasion "local regulations, rules and other measures were issued by local governments at the provincial, city and county levels acting within their respective constitutional powers and functions and applied at their corresponding local level."<sup>90</sup>

China's representative does state, however, that "sub-national governments have no

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<sup>89</sup> Worker rights, 19 U.S.C. § 2901, accessed March 14, 2012, [http://frwebgate.access.gpo.gov/cgi-bin/usc.cgi?ACTION=RETRIEVE&FILE=\\$\\$xa\\$\\$busc19.wais&start=4837958&SIZE=36697&TYPE=PDF](http://frwebgate.access.gpo.gov/cgi-bin/usc.cgi?ACTION=RETRIEVE&FILE=$$xa$$busc19.wais&start=4837958&SIZE=36697&TYPE=PDF).

<sup>90</sup> "Report of the Working Party on the Accession of China," World Trade Organization, November 13, 2001, p. 14, accessed March 18, 2012, [http://tcc.export.gov/Trade\\_Agreements/WTO\\_Agreements/WTO\\_China\\_AG.asp](http://tcc.export.gov/Trade_Agreements/WTO_Agreements/WTO_China_AG.asp).

autonomous authority over issues of trade policy to the extent that they were related to the WTO Agreement and the Draft.”<sup>91</sup>

To that end, China’s representative and the Working Party of the WTO agreed upon a mechanism through which entities could report violations of the WTO Agreement: “All individuals and entities could bring to the attention of central government authorities cases of non-uniform application of China’s trade regime, including its commitments under the WTO Agreement and the Draft Protocol.”<sup>92</sup> What becomes clear here is that, pursuant to policies over which sub-national governments have no authority, violation reports should be handled through the central national government. There are no prohibitions, however, of individuals and entities working with sub-national governments on issues over which those local governments do have authority. In fact, it would seem by China’s representative’s fierce defense of the jurisdiction of sub-national governments that the central Chinese government supports a level of autonomy and self-sufficiency. To this end, it does not appear that there are any trade agreement barriers to the United States working directly with local government officials on legal and economic issues over which the local governments have jurisdiction.

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<sup>91</sup> “Report of the Working Party on the Accession of China,” p. 13.

<sup>92</sup> “Report of the Working Party on the Accession of China,” p. 14.

### **Chapter III: Proposal of New Laws**

Because existing laws are inadequate to deter and remedy foreign labor abuse, this paper proposes two new laws. The first is a corporate tax incentive, issued upon the fulfillment of a set of labor standards, that will encourage voluntary compliance. These guidelines combine conditions demanded by the China Labor Law with criteria derived from economic data. The second proposal introduces a law parallel to the Alien Tort Statute which will give jurisdiction to United States courts to oversee cases filed by foreign workers against U.S. corporations which commit violations of foreign labor laws. This chapter concludes with a brief evaluation of the economic impacts of these new laws.

#### **Part One: Constructing the Tax Credit**

The tax incentive for compliance will be the stronger of the two legal mechanisms for providing adequate standards and rights for foreign workers. The primary goal is to make the incentive large enough not only to outweigh compliance costs, but also to make compliance more profitable for U.S. corporations than noncompliance. Of the two potential tax incentives - tax deductions and tax credits - tax credits will be the most effective at accomplishing this goal. A tax credit directly reduces the amount of taxes an individual or corporation has to pay, as opposed to a tax deduction, which reduces the

amount of taxable income claimed.<sup>93</sup> A corporation that complies with the standards suggested below will earn a per-worker tax credit that will directly reduce the corporation's yearly taxes. The value of the credit will be discussed later; first, the standards that corporations would have to meet to procure this tax credit must be outlined.

Given the significance of Chinese labor to U.S. manufacturers and the availability of regulatory data discussed in Chapter 1, Chinese labor law provides a baseline standard. Chinese labor law is primarily codified in the Labor Law of 1994 and the Labor Contract Law of 2008. China legislates a minimum wage, which is governed by two standards: monthly and hourly. There is no national minimum wage; standards are set at the provincial and municipal level.<sup>94</sup> Factories are prohibited from contracting with workers for wages that are below the local minimum wage standard.<sup>95</sup> Because the minimum wage is set by local governments, it is different in nearly every area of China. For example, Shanghai's minimum wage is RMB 1,120/month, or about \$165, but in Chongqing the minimum wage is only RMB 870/month, or roughly \$130.<sup>96</sup> It is important to note that even when adjusted for relative prices and costs of living, China's various minimum wages are much lower than in Western Europe and America.<sup>97</sup>

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<sup>93</sup> "Tax Deduction vs. Tax Credit," *The Tax Break: The TurboTax Blog*, November 17, 2009, <http://blog.turbotax.intuit.com/2009/11/17/tax-deduction-vs-tax-credit/>.

<sup>94</sup> Labor Law of the People's Republic of China, Article 48, July 5, 1994, Order Number 28, Eighth National People's Congress, <http://www.usmra.com/china/Labour%20Law.htm>.

<sup>95</sup> Nathan Jackson, "What Are the Major Aspects of Chinese Labor Law," *The University of Iowa Center for International Finance and Development*, April 2011, p. 4, accessed March 3, 2012, <http://blogs.law.uiowa.edu/ebook/uicifd-ebook/what-are-relevant-issues-concerning-chinese-labor-and-employment-law>.

<sup>96</sup> Jackson, "What Are the Major Aspects of Chinese Labor Law," p. 4.

<sup>97</sup> Jackson, "What Are the Major Aspects of Chinese Labor Law," p. 4.

Some of the most frequently broken rules in China's Labor Law are those that cover overtime.<sup>98,99,100,101</sup> The two most important of these rules are the limit on overtime hours and the minimum compensation for overtime. Recall from Chapter I that, according to China's Labor Law, workers cannot work more than 40 hours per week without receiving overtime compensation, and that a factory cannot require more than 36 hours per month.<sup>102</sup> The following table, also in Chapter I, shows the rules governing overtime pay in China's Labor Law:

<b>Extended Working Hours</b>	<b>Minimum Overtime Pay (percent of regular wages)</b>
Typical working day	150 percent
Rest day (min. one per week) (i.e., weekend)	200 percent
National holiday	300 percent

Based on this scale, workers should be getting paid a minimum of 150% of their regular wages for a maximum of 36 hours of overtime per month.

China's labor laws also have provisions covering workplace safety. Factories are required to pay the medical expenses of injuries, disability, and occupational diseases through each province's Work-Related Injury Insurance Regulations.<sup>103</sup> All employers are required to pay the premiums for the insurance fund, even though not all do. There are no

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<sup>98</sup> "Tragedies of Globalization: The Truth Behind Electronics Sweatshops," *China Labor Watch*, July 12, 2011, pp. 7-134, <http://chinalaborwatch.org/pdf/20110712.pdf>.

<sup>99</sup> "Wal-Mart Standards Fail, Workers Suffer," *China Labor Watch*, November 25, 2009, pp. 3-21, <http://www.chinalaborwatch.org/pdf/20091125.pdf>.

<sup>100</sup> "An Investigation of Suppliers of Dollar General," *China Labor Watch*, August 10, 2010, pp. 3-6, [http://www.chinalaborwatch.org/upfile/2010\\_11\\_3/20101131312392.pdf](http://www.chinalaborwatch.org/upfile/2010_11_3/20101131312392.pdf).

<sup>101</sup> "Investigation of Two Clothing and Apparel Factories in China," *China Labor Watch*, November 29, 2011, pp. 4-22, <http://www.chinalaborwatch.org/pdf/20111129-final.pdf>.

<sup>102</sup> Labor Law of the People's Republic of China, Article 41.

<sup>103</sup> Jackson, "What Are the Major Aspects of Chinese Labor Law," p. 7.

mechanisms for opting out of the Work-Related Injury Insurance systems. The Labor Law requires factories to inform potential workers of any occupational hazards before getting those workers to sign contracts, as well as requiring factories to provide workers with safe and clean working conditions.<sup>104</sup>

Penalties for violations of these safety laws are tricky, and it starts with the fact that the system relies heavily on workers themselves reporting safety violations. Despite having stipulations to protect the jobs of workers who report violations, many workers do not feel secure enough to report grievances.<sup>105</sup> In instances where reports are made, the civil courts punish factories through warnings, fines, and workplace closures.<sup>106</sup>

Unions are allowed in China, and are in fact easy to organize. All one needs is 25 workers to join the union and the factory is usually required to grant the request.<sup>107</sup> That said, unions perform a much different function in Chinese society than in many other countries. In China, the primary purpose of unions is not to support the interests of their workers, but rather to keep workers happy and prevent unrest.<sup>108</sup> Unions try to deter common workers from striking or filing grievances, and instead try to strike deals with

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<sup>104</sup> Labor Law of the People's Republic of China, Chapter 6.

<sup>105</sup> Jackson, "What Are the Major Aspects of Chinese Labor Law," p. 8.

<sup>106</sup> Jackson, "What Are the Major Aspects of Chinese Labor Law," p. 8.

<sup>107</sup> Jackson, "What Are the Major Aspects of Chinese Labor Law," pp. 10-12.

<sup>108</sup> Jackson, "What Are the Major Aspects of Chinese Labor Law," p. 10.

employers at a national level through the All-China Federation of Trade Unions, of which all unions are required to be a part.<sup>109,110</sup>

Chinese law also addresses child labor. Under the child labor regulations section of the China Labor Law of 1994, employers are prohibited from recruiting, employing, or facilitating the employment of children under the age of sixteen.<sup>111</sup> Between the ages of sixteen and eighteen, workers are considered under-aged and cannot work in mining, unhealthy or hazardous work, or high-intensity work.<sup>112</sup> While these statutes have proven to be an improvement to child protection, these regulations are still not adequately enforced and therefore have not been completely effective in eliminating child labor.<sup>113</sup>

Chinese labor law also governs discrimination and contracts. The Labor Law prohibits employment discrimination on the basis of gender, and the Employment Promotion Law of 2007 prohibits employment discrimination on the basis of gender, ethnicity, disability, disease, and rurality.<sup>114</sup> The Labor Contract Law mandates that factories must provide employees with contracts that outline the terms of employment,

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<sup>109</sup> Edward J. Epstein, "China's New Labor Contract Law: Overview and Recommended Action Steps for Employers," *Troutmann Sanders LLP*, p. 7, accessed March 5, 2012, <http://www.troutmansanders.com/files/Publication/da0358e9-71d3-4370-82dc-5344756922ba/Presentation/PublicationAttachment/99cc8c35-65ae-4be2-b84e-63fec7baa708/TS%20China%20New%20Labor%20Contract%20Law%20Overview.pdf>.

<sup>110</sup> Jackson, "What Are the Major Aspects of Chinese Labor Law," p. 10.

<sup>111</sup> Labor Law of the People's Republic of China, Article 15.

<sup>112</sup> Labor Law of the People's Republic of China, Article 54.

<sup>113</sup> Jackson, "What Are the Major Aspects of Chinese Labor Law," pp. 9-10.

<sup>114</sup> Employment Promotion Law of the People's Republic of China, Article 3, August 30, 2007, Order Number 70, 10th National People's Congress, [http://www.baliprocess.net/files/China/China\\_employment%20promotion%20law\\_2008-eng.pdf](http://www.baliprocess.net/files/China/China_employment%20promotion%20law_2008-eng.pdf).

job description, place of work, working hours, rest and leave periods, wages, social insurance, labor protections, and description of working conditions.<sup>115</sup>

Compliance with Chinese labor law provides a useful starting point for tax credit guidelines, although, with respect to some issues discussed below, more stringent standards are necessary. On the issues of overtime hours, overtime pay, safety, unions, child labor, discrimination, and contracts, China's labor laws are sufficient in their conception, albeit poorly enforced (which is a topic that will be discussed later). The primary areas where China's labor laws are inadequate are the minimum wage, which is too low to meet the living needs of workers, and enforcement, which is ineffective.

China's practice of determining minimum wage at a local level, using relative prices and costs of living, is quite effective and efficient, but the minimum wage in each region should be, at the very least, enough to cover the cost of living. To propose a new minimum wage standard for this tax credit, it is important to know what the cost of living in the region in which each factory is located. As has already been discussed in Chapter I, consumption expenditure will be substituted for cost of living in this endeavor. This table shows the regional values of per capita consumption expenditure and regional minimum wage:<sup>116,117,118</sup>

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<sup>115</sup> Jackson, "What Are the Major Aspects of Chinese Labor Law," pp. 15-18.

<sup>116</sup> "Tragedies of Globalization: The Truth Behind Electronics Sweatshops," p. 99.

<sup>117</sup> Compiled data from the National Bureau Of Statistics of the The Peoples Republic Of China, "Household Consumption Expenditure," accessed March 5, 2012, [http://www.allcountries.org/china\\_statistics/3\\_18\\_household\\_consumption\\_expenditure.html](http://www.allcountries.org/china_statistics/3_18_household_consumption_expenditure.html).

<sup>118</sup> Fair Wage Network, "2011: Minimum Wage Adjustments of Chinese Provinces/Municipalities," accessed March 5, 2012, <http://fair-wage.com/en/fair-wage-observatory/new-legal-provisions/101-2011-minimum-wage-adjustments-of-chinese-provincesmunicipalities-.html>.



LOCATION OF FACTORY	CONSUMPTION EXPENDITURE	MINIMUM WAGE
Shenzhen	\$242.70	\$173.89
Longhua	\$242.70	\$173.89
Guanlan	\$242.70	\$173.89
Dongguan	\$248.83	\$174.27
Suzhou	\$277.39	\$180.61
Kunshan	\$305.38	\$180.61
Zhuhai	\$203.38	\$174.27
Shanghai	-	\$177.44
Zhongshan	-	\$174.27
Zhejiang	\$180.61	\$174.27
Huasheng	\$180.61	\$174.27

It is clear from this data that in every relevant region the minimum wage is below the per capita consumption expenditure, and in three areas - Dongguan, Suzhou, and Kunshan - the minimum wage is significantly sub-par, with a difference of as much as \$124.77, or 69% of the minimum wage. For the minimum wage standard for this tax credit, then, a corporation should ensure that its factories are paying wages equal to 125% of the per capita consumption expenditure. The additional 25% is to help account for the difference between consumption expenditure and cost of living. This is a table showing the minimum wages that corporate-commissioned factories should be paying, if the corporation wishes to receive the tax credit:

LOCATION OF FACTORY	CONSUMPTION EXPENDITURE	REGIONAL MINIMUM WAGE	TAX CREDIT MINIMUM WAGE
Shenzhen	\$242.70	\$173.89	\$303.38
Longhua	\$242.70	\$173.89	\$303.38
Guanlan	\$242.70	\$173.89	\$303.38
Dongguan	\$248.83	\$174.27	\$311.04
Suzhou	\$277.39	\$180.61	\$346.74
Kunshan	\$305.38	\$180.61	\$381.73
Zhuhai	\$203.38	\$174.27	\$254.23
Shanghai	-	\$177.44	\$225.76
Zhongshan	-	\$174.27	\$225.76
Zhejiang	\$180.61	\$174.27	\$225.76
Huasheng	\$180.61	\$174.27	\$225.76

The tax credit minimum wages for Shanghai and Zhongshan are estimations. Since it was difficult to locate data on the per capita consumption expenditure in every region, an estimation can be made using the similarities in regional minimum wages between those two regions and the Zhejiang region. This is a poor estimation, given that there is no discernible link or pattern between consumption expenditure and regional minimum wage, but it will be suitable for this tax credit and an accurate wage could be computed with better data acquisition.

Enforcement is also a problem for China's labor laws. Enforcement is primarily left to local government administrators and safety boards who lack the training necessary for effective factory monitoring.<sup>119</sup> Moreover, due to the central government's policy of rewarding local leaders who grow the local economy, there is a serious conflict of interest

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<sup>119</sup> Jackson, "What Are the Major Aspects of Chinese Labor Law," pp. 18-19.

when it comes to enforcing some of these laws and regulations.<sup>120</sup> If falsifying a factory audit guarantees that the factory continues to function well in the economy, some local officials feel they have more to gain from lying than from telling the truth. These problems are compounded by the fact that when labor laws are written to cover all employers, all employers must be monitored. The regulatory system is overburdened and under prepared in this fashion. One of the advantages to implementing a U.S. tax credit is that compliance is not mandatory, and thus the monitoring burden is mitigated. Corporations that wish to receive the credit will be motivated and, in fact, required to self-regulate and self-report. Monitoring by local officials, which in the new system would be less biased than self-reporting by corporations, will still be done on a routine basis and when compliance is in doubt, but a combination of systemic changes and corporate self-motivation will increase the effectiveness of this monitoring.

The first step toward more effective monitoring must involve non-governmental organizations (NGOs). Many NGOs, including those from America, China, and international cooperatives, have been extremely effective at gathering information about the treatment of factory workers.<sup>121, 122, 123, 124, 125, 126</sup> In the reports that were studied for this thesis, this information has been gathered through two primary methods: extensive

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<sup>120</sup> Jackson, "What Are the Major Aspects of Chinese Labor Law," p. 18.

<sup>121</sup> "Tragedies of Globalization: The Truth Behind Electronics Sweatshops."

<sup>122</sup> "Workers as Machines: Military Management in Foxconn."

<sup>123</sup> "Wal-Mart Standards Fail, Workers Suffer."

<sup>124</sup> "Wal-Mart's Road to Sustainability: Paved with False Promises?," *China Labor Watch*, July 27, 2009, [http://www.chinalaborwatch.org/investigations/2009\\_07\\_27/Walmart%20Report.pdf](http://www.chinalaborwatch.org/investigations/2009_07_27/Walmart%20Report.pdf).

<sup>125</sup> "An Investigation of Suppliers of Dollar General."

<sup>126</sup> "Investigation of Two Clothing and Apparel Factories in China."

interviews with a multitude of workers at each factory being investigated, and infiltration of the factory, where an employee of the NGO disguises himself as a worker, gains employment at the factory, and reports his findings. Usually the undercover investigation is done to confirm the information gathered in interviews.

Reports by NGOs have been used to effectively spur changes in corporate behavior. Examples of this are the China Labor Watch and Students & Scholars Against Corporate Misbehavior reports on Foxconn's factories in China.<sup>127,128</sup> Apple has made it a major priority to change the conditions of the workers producing their products at these factories,<sup>129</sup> and even pressured Foxconn to open its doors to American reporters, so that a full perspective could be gained on labor conditions. For examples of how local Chinese NGOs have effected change, one can look to the example of "The Other Side of Apple: Pollution Spreads Through Apple's Supply Chain," a report issued by a coalition of local Chinese NGOs that was subsequently cited several times by the New York Times, spurring serious condemnations from activists and businessmen alike.<sup>130</sup> One could also use the example of "China's Youth Meet Microsoft," a report by the National Labor Committee based on intelligence gathered by a local watchdog group, which caused

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<sup>127</sup> "Tragedies of Globalization: The Truth Behind Electronics Sweatshops."

<sup>128</sup> "Workers as Machines: Military Management in Foxconn."

<sup>129</sup> Kristin Huguet and Carolyn Wu, "Fair Labor Association Begins Inspections of Foxconn," *Apple Press Info*, February 13, 2012, accessed March 5, 2012, <http://images.apple.com/pr/library/2012/02/13Fair-Labor-Association-Begins-Inspections-of-Foxconn.html>.

<sup>130</sup> Amy Westervelt, "How Local Watchdog Groups, Not Western Companies, Are Shaping Business Practices in China," *Forbes*, December 06, 2011, accessed March 5, 2012, <http://www.forbes.com/sites/amywestervelt/2011/12/06/how-local-watchdog-groups-not-western-companies-are-shaping-business-practices-in-china/>.

several companies to threaten to take their business elsewhere from the implicated factory, KYE, and to immediately send auditors to the factory.<sup>131</sup>

These examples help prove the point that NGOs are a significant resource in the monitoring of factories. How to incorporate them into the enforcement system is a more complicated question. Even with the reduced need for monitoring in the tax credit system, it is unlikely that there are enough NGOs with sufficient resources to monitor factories full-time. Nor can it be assumed that NGOs would agree to do so; many are multi-faceted organizations that investigate and issue reports on a variety of issues. The U.S. government cannot expect to get all of its monitoring done by NGOs. It is likely, though, that the United States could get some of the more effective NGOs to agree to train local Chinese officials on the proper ways to conduct audits and interviews. With proper training, half of the barrier to effective governmental monitoring is removed.

The other half of the problem is the conflict of interest in officials who are responsible for both enforcing labor laws and improving the local economy. If it is explained to these officials that the local economy can only benefit from the effective factory monitoring required for this tax credit, much of this conflict of interest will be mitigated. The previous claim is true: companies seeking the tax credit would demand that its factories improve worker conditions, which would include increased safety and wages. This increased safety would reduce the burden on provincial insurance programs, and the increased wages would increase local consumption. On top of that, the corporation would be paying the factories more, so again, increase consumption and

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<sup>131</sup> Westervelt, "How Local Watchdog Groups, Not Western Companies, Are Shaping Business Practices in China."

GDP. The corporation, which is incurring increased costs from the factory, would file a report about improved worker conditions based on information provided by the factory. Then the corporation would request that the improved worker conditions be verified by a local audit, in order to offset the costs with the tax credit. If the local auditors confirm that the factory meets the necessary conditions, the corporation will continue to ensure that the workers are treated well. If the auditors deny the factory approval, corporations, confused both about their increased costs despite the failed audit and about faulty information provided to them by the factory, will likely continue to demand that the factory increase worker conditions until it passes the audit and the corporation gets its tax credit. Even in the event that the corporation decides to cut its losses and quit its pursuit of the tax credit, because the factory had not adequately improved worker conditions, the return of worker conditions to their original state is not a significant change. In other words, at worst, conditions would remain the same. In this situation, auditors have nothing to gain by lying on the audit reports and nothing to lose by telling the truth in an audit report. This is a fundamentally different situation than the status quo, in which local officials do have incentives to lie on audits. This mitigation of the conflict of interest in local administrators is vital to the effectiveness of monitoring.

One major criticism of this argument on enforcement is that local Chinese officials may not be willing to perform audits for the fulfillment of a U.S. tax credit. This is a serious issue for this thesis, one for which there is not a perfect answer. The strongest response relies heavily on the argument in the previous paragraph: local government officials stand to benefit significantly from corporations pursuing this tax credit. The

existence and easy fulfillment of this tax credit will increase local economies and decrease the burden on the local enforcement systems. This, combined with increased training and efficiency and reduced conflict of interest between enforcement and economy should be more than enough motivation to get local administrators on board with the plan. There is also an argument to be made that these local officials must audit the factories either way to check for compliance with China's Labor Law; it would not cost them much to consider the additional tax credit standards during a regular audit, and as previously stated, local officials stand to gain much from doing so.

For factories to meet the standards set forth, they will have to take a number of measures. Each factory will have to increase the normal and overtime wages of each worker, increase worker safety, decrease child labor, and increase its workforce in order to reduce the number of overtime hours each employee has to work. Some of these will increase the cost of running the factory, and others will not. The aim is to calculate the per-worker increase in cost that each of these factories would incur to meet the tax credit labor standards, and then translate that into the amount extra that U.S. corporations will have to pay these factories for their goods.

The best place to start is the most complicated: increasing wages to meet the new standard of 125% of per capita consumption expenditure. Here is a table showing the monthly differences between local per capita consumption expenditure, regional

minimum wage, current factory minimum wage, and the new tax credit minimum wage:

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FACTORY	PROVINCE	CONSUMPTION EXPENDITURE	REGIONAL MINIMUM WAGE	CURRENT FACTORY MINIMUM WAGE	TAX CREDIT MINIMUM WAGE
Hongkai Electronics	Dongguan	\$248.83	\$174.27	\$169.40	\$311.04
Catcher Technology	Suzhou	\$277.39	\$180.61	\$175.56	\$346.74
Kunshan Compal	Kunshan	\$305.38	\$180.61	\$175.56	\$381.73
Flextronics	Zhuhai	\$203.38	\$174.27	\$202.51	\$254.23
Foxconn Kunshan	Kunshan	\$305.38	\$180.61	\$235.62	\$381.73
Foxconn Longhua	Shenzhen	\$242.70	\$173.89	\$184.80	\$303.38
Dashing Decoration	Dongguan	\$248.83	\$174.27	\$113	\$311.04
Stanley Tool	Zhongshan	-	\$174.27	\$115	\$225.76
Huasheng Packaging Factory	Huasheng	\$180.61	\$174.27	\$102.98	\$225.76
Yiu Yi Plastic & Mould	Shenzhen	\$242.70	\$173.89	\$129	\$303.38

With the exception of Flextronics and the two Foxconn locations, every factory's minimum wage is below that of the regional minimum wage. Since every regional minimum wage is below the tax credit minimum wage, many of these factories will incur

<sup>132</sup> "Tragedies of Globalization: The Truth Behind Electronics Sweatshops," pp. 5-136.

<sup>133</sup> "Workers as Machines: Military Management in Foxconn," pp. 6-24.

<sup>134</sup> "Wal-Mart Standards Fail, Workers Suffer," pp. 3-21.

<sup>135</sup> "Wal-Mart's Road to Sustainability: Paved with False Promises?" pp. 3-27.

<sup>136</sup> "An Investigation of Suppliers of Dollar General," pp. 3-13.

<sup>137</sup> "Investigation of Two Clothing and Apparel Factories in China," pp. 4-22.



substantial wage increases if the corporations demand that the factories meet the tax credit standard. One factory - Dashing Decoration, which supplies Wal-Mart - would have to increase wages by 275%.

To get a better idea of the per-worker wage increase at each factory, here is another table that illustrates the differences between the current factory minimum wages and the tax credit wages:

<b>FACTORY</b>	<b>CURRENT FACTORY MINIMUM WAGE</b>	<b>TAX CREDIT MINIMUM WAGE</b>	<b>DOLLAR DIFFERENCE</b>	<b>PERCENT DIFFERENCE</b>
Hongkai Electronics	\$169.40	\$311.04	\$141.64	184
Catcher Technology	\$175.56	\$346.74	\$171.18	198
Kunshan Compal	\$175.56	\$381.73	\$206.17	217
Flextronics	\$202.51	\$254.23	\$51.72	126
Foxconn Kunshan	\$235.62	\$381.73	\$146.11	162
Foxconn Longhua	\$184.80	\$303.38	\$118.58	164
Dashing Decoration	\$113	\$311.04	\$198.04	275
Stanley Tool	\$115	\$225.76	\$110.76	196
Huasheng Packaging Factory	\$102.98	\$225.76	\$122.78	219
Yiu Yi Plastic & Mould	\$129	\$303.38	\$174.38	235

Clearly, these factories - which represent only a small number and range of factories in China - will have to significantly increase wages per worker. One could then go into detail about the number of workers at each factory and, therefore, the total increase in wages for each factory, but the workforce size varies drastically from factory to factory,

and for the purposes of a broad, general tax credit, per-worker costs are best. Amongst these ten factories - which represent suppliers from electronics, retail, and apparel - the average per-worker increase in wages is \$144.14 per month. The highest is \$205.88, and the lowest is \$51.72. These numbers will become more important after evaluating the costs of meeting the other major standards of this tax credit.

The next important standard to cover is that of overtime, both in the number of hours and the wage paid per overtime hour. Every factory covered has periods where the number of overtime hours per month exceeds the federal limit of 36, although one factory - Flextronics - has a low-period where workers only work around 20 overtime hours per month. Though the data is scarce regarding the specific per-hour overtime wage at each factory, some estimations can be made. Here is a table illustrating the differences between factory overtime hours and wages and tax credit overtime hours and wages:<sup>138,139,140, 141, 142, 143</sup>

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<sup>138</sup> “Tragedies of Globalization: The Truth Behind Electronics Sweatshops,” pp. 5-136.

<sup>139</sup> “Workers as Machines: Military Management in Foxconn,” pp. 6-24.

<sup>140</sup> “Wal-Mart Standards Fail, Workers Suffer,” pp. 3-21.

<sup>141</sup> “Wal-Mart’s Road to Sustainability: Paved with False Promises?” pp. 3-27.

<sup>142</sup> “An Investigation of Suppliers of Dollar General,” pp. 3-13.

<sup>143</sup> “Investigation of Two Clothing and Apparel Factories in China,” pp. 4-22.

<b>FACTORY</b>	<b>AVERAGE OVERTIME HOURS</b>	<b>AMOUNT OVER FEDERAL LIMIT</b>	<b>FACTORY OVERTIME WAGE</b>	<b>TAX CREDIT OVERTIME WAGE</b>
Hongkai Electronics	60 - 120	24 - 84	-	\$2.92/hr
Catcher Technology	75	39	-	\$3.25/hr
Kunshan Compal	40	4	\$1.18/hr	\$3.58/hr
Flextronics	20 - 130	0 - 94	-	\$2.38/hr
Foxconn Kunshan	45	9	-	\$3.58/hr
Foxconn Longhua	40	4	-	\$2.84/hr
Dashing Decoration	80	44	\$.44/hr	\$2.92/hr
Stanley Tool	40	4	-	\$2.12/hr
Huasheng Packaging Factory	70	34	\$.71/hr	\$2.12/hr
Yiu Yi Plastic & Mould	100 - 300	64 - 264	\$1.11/hr	\$2.84/hr

To meet the tax credit standard, every factory will have to increase its overtime wages and decrease the number of overtime hours it requires of its workers. Though there is only data for the per-hour overtime wages in four of these factories, it is nearly certain that the tax credit overtime wage is over double the current overtime wage at every factory. Still, if it is assumed that, for each of the six factories with missing data, the tax credit overtime wage was exactly double the current overtime wage, then the average difference between the current overtime rate and the tax credit overtime rate is \$1.45 per hour. At the federal maximum of 36 overtime hours per month, this value is \$52.20 per worker. This is, again, an over-estimation, but will suffice for the stated purposes.

To maintain production levels while simultaneously reducing the number of required overtime hours to 36 per month, factories will have to employ more workers. If each factory hires the exact number of new workers needed to offset the difference between the federal mandate of 36 hours per month and any excessive overtime, most factories will actually save money. This is because most of these factories - the only exception being Dashing Decorations - pay more per hour for overtime than they do for regular hours. If each factory adopted the tax credit normal and overtime wage standards, every factory would save substantial amounts of money by limiting the overtime of each worker. So, more workers at regular hours actually cost less money than fewer workers at high numbers of overtime hours. The difference between these two values is difficult to quantify given all of the variables with each factory, so for the purposes of this calculus, one should simply consider the exchange of more workers at less overtime for fewer workers at greater overtime of little financial significance.

The problem with this argument is that not every factory can, at present, hire more workers. There are barriers in place preventing them from doing so. One such barrier is a lack of infrastructure to support more workers - perhaps every workstation is filled, and the only way to increase production is to increase overtime hours per worker. This is an issue that will be taken into account shortly, in the harder-to-quantify section of potential expenses. Another potential barrier is that new workers can be difficult to procure given the poor working conditions and poor reputations of these factories. It would not be a stretch to say that if a factory were increasing its labor standards, it would be much easier to attract workers. Such labor-friendly factories would be attractive both to workers who

have never worked in factories before and those workers who are currently employed by an abusive factory. Many of these barriers to recruitment can thus be mitigated.

There are several other factors that are difficult to quantify, including increased workplace safety and improvement of infrastructure for the purposes of an expanding workforce. As has been mentioned before, this thesis is interested in developing a general tax credit that could be applied to every factory, and some of these issues would be factory specific. Every factory's safety and infrastructure levels are different in the status quo, so every factory will have to spend a different amount to meet the tax credit standard. What is needed is a broad estimation of the kinds of costs that would be incurred per worker for these improvements. A reasonable estimation would seem to be just over half of the average necessary per-worker pay increase - \$75, but instead of per month it will be per quarter. Considering that even the smallest of the six electronics factories listed has over 1000 workers, \$75 per worker per quarter would manifest itself in \$300,000 in safety and infrastructure improvements per year. Given the purchasing power of a U.S. dollar in many of these regions, that estimation is more than reasonable. Since the measurements need to remain consistent, this must be converted into a per-worker per-month cost - \$25. It is important to note that these safety and infrastructure improvements would largely be a one-time investment. Most factories will not need to make \$300,000 per year in improvements for more than one year. Once the improvements are made, these costs should no longer be an issue.

With all of the major necessary costs of meeting the new tax credit standard outlined, they need to be summed. Taking the average costs of improved normal wages

and overtime wages and the cost of safety and infrastructure improvements, one gets \$226.78 per worker per month for the first year, at which point the safety and infrastructure improvements can be factored out. The average values are unhelpful in this situation, though, because if one constructed a tax credit based on the average costs, then half of all corporations would find it unprofitable to meet the standards. Instead, the highest values should be taken, and with those numbers one gets \$320.16 per worker per month. For a factory of 1000 workers, this is a per year cost of \$3,841,920.

It is necessary to make this tax credit as appealing as possible to as many U.S. corporations as possible, so it stands to reason the credit should be well-above even the highest per-worker cost incurred. A tax credit of \$500 per month for every worker in these improved conditions ought to be effective. For a corporation commissioning a factory of 1000 workers, that is a \$6,000,000 per year tax credit for the first year. When you subtract this from the cost calculated in the previous paragraph, the profit for the corporation comes out to \$2,158,080 per year. Once the safety and infrastructure improvements are factored out, the corporation would make a profit of \$2,458,080 per year. This amount alone may not be enough to entice the larger corporations like Wal-Mart to comply, but those larger corporations have dozens of factories with tens of thousands of workers. A corporation that commissioned ten factories with 1000 workers in each factory could make a profit of \$24,580,800. Because this tax credit is general enough that it can be scaled based on the number of factory workers employed, it can entice corporations of any size.

## **Part Two: Expanding the Alien Tort Statute**

The second approach to alleviating these labor abuses is an expansion of the Alien Tort Statute (ATS). The ATS was part of the Judiciary Act of 1789, and says that, “The district courts shall have original jurisdiction of any civil action by an alien for a tort only, committed in violation of the law of nations or a treaty of the United States.”<sup>144,145</sup> The problem with the ATS as it is currently written is that it only gives U.S. courts jurisdiction over cases filed by aliens over internationally agreed upon torts; commissioning a factory that violates labor laws local to the factory is not considered such a tort. There are three possible solutions to expanding U.S. court jurisdiction to cover this issue: directly amend the ATS to cover the commission of a factory which violates its local labor laws in addition to torts, craft a law parallel to the ATS that gives courts such jurisdiction, or make the commission of such a factory a statutory tort in U.S. law and a violation of U.S. treaties. All three of these courses lead to the same ultimate conclusion: foreign laborers will gain the right to sue U.S. corporations in American courts for failing to guarantee that the laborers work in legal conditions as set by the laborers’ native country.

Because all three options serve the final purpose of giving courts jurisdiction in this circumstance, it would seem to matter little which is chosen. All three require legislative action, just like the aforementioned tax credit, so there is little difference there. There is, however, a significant semantic difference between the first two options -

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<sup>144</sup> The Judiciary Act of 1789, Chapter 20, 1 Statute 73, 1st Congress, accessed March 8, 2012, [http://www.constitution.org/uslaw/judiciary\\_1789.htm](http://www.constitution.org/uslaw/judiciary_1789.htm).

<sup>145</sup> Alien’s Action for Tort, 28 U.S.C. § 1350, accessed March 8, 2012, [http://frwebgate.access.gpo.gov/cgi-bin/usc.cgi?ACTION=RETRIEVE&FILE=\\$xa\\$busc28.wais&start=2639306&SIZE=4129&TYPE=PDF](http://frwebgate.access.gpo.gov/cgi-bin/usc.cgi?ACTION=RETRIEVE&FILE=$xa$busc28.wais&start=2639306&SIZE=4129&TYPE=PDF).

amending the ATS or creating a parallel law to ATS - and the third option - making the commission of a delinquent factory a statutory tort and a violation of treaties. The first two options do not make it a U.S. crime to commission a factory that violates its local labor laws, they just give the U.S. courts jurisdiction to hear a case about the violation of said labor laws which is filed by a foreign worker against a U.S. corporation. The courts only have such jurisdiction because the corporation is American, not because there was a violation of U.S. law. The third option actually makes it a federal crime for U.S. corporations to commission factories that break foreign labor laws. This is a much stronger stance on the situation, as well as a complex legal issue. There is precedent, however, for making the violation of foreign laws a crime in the United States - the Lacy Act. According to the Lacy Act, it is a felony in the United States “to import, export, transport, sell, receive, acquire, or purchase in interstate or foreign commerce - (A) any fish or wildlife taken, possessed, transported, or sold in violation of any law or regulation of any State or in violation of any foreign law...”<sup>146</sup> It is clear from this that for over a century the United States has made the violation of foreign laws a federal crime. The Lacy Act was even amended in 2008, and that particular section was left completely intact, so as recently as four years ago Congress was still in support of this practice.<sup>147</sup>

The examination of the Lacy Act presents a new option to this scenario. The Lacy Act introduces an import regulation that hinges around the violation of foreign laws. A similar approach could be taken with the delinquent factories: it could be made a felony

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<sup>146</sup> The Lacy Act of 1900, 16 U.S.C. §§3371-3378, 56th Congress, accessed on March 9, 2012, <http://www.fws.gov/le/pdf/Lacey.pdf>.

<sup>147</sup> Amendments to the Lacy Act from H.R.2419, Sec. 8204, 110th Congress, accessed on March 9, 2012, <http://www.eia-global.org/PDF/background--redlinedLaceyamndmnt--forests--may08.pdf>.



to import any product that was manufactured in a factory which breaks any foreign labor laws. As discussed in Chapter II, this is not a reasonable or practical approach to the labor abuse problem; there are substantial and unworkable enforcement and economic problems with such a plan. Furthermore, there is significant criticism of the Lacy Act, because there is no list of all the relevant foreign laws with which a company or individual is responsible for compliance.<sup>148</sup> Nearly 9,000 laws relevant to the Lacy Act exist in Indonesia alone; similarly, there will be thousands of laws pertinent to factory labor conditions in all of the countries in which there are factories. It will virtually impossible for a large multinational corporation like Wal-Mart to guarantee compliance for every one of its factories. For all of these reasons, that path is not a viable option.

That still leaves the original three options - amend the ATS, create a law parallel to the ATS, or make the commission of a delinquent factory a statutory tort and a violation of treaties. Because of the aforementioned complexities and controversies involved with making the violation of foreign laws a U.S. crime, it would be best to avoid option three. Of the remaining two options, the creation of a law parallel to the ATS is more viable. The ATS is an untouched statute from the Judiciary Act of 1789 - the very act that created the U.S. federal judiciary.<sup>149</sup> As such, it is a statute of rich legal heritage; it would be best to leave it unaltered. This leaves only one option, the creation of a law parallel to the ATS which would give jurisdiction to U.S. courts in cases filed by aliens

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<sup>148</sup> "2008 GAC Position Papers," *National Customs Brokers & Forwarders Association of America*, accessed on March 9, 2012, [http://www.ncbfaa.org/Scripts/4Disapi.dll/4DCGI/cms/review.html?Action=CMS\\_Document&DocID=11480&MenuKey=pubs](http://www.ncbfaa.org/Scripts/4Disapi.dll/4DCGI/cms/review.html?Action=CMS_Document&DocID=11480&MenuKey=pubs).

<sup>149</sup> The Judiciary Act of 1789.

against corporations which commission factories that violate foreign labor laws. For the purposes of this thesis, this law will be referred to as the Alien Labor Statute (ALS).

Upon arriving at this decision, the ATS analysis from Chapter II becomes much more relevant. It also becomes necessary to recognize potential barriers to the use of the ATS and this new Alien Labor Statute. Only after looking at each of these thoroughly can it be decided if crafting such a law is a worthwhile endeavor.

Despite the fact that between 1789 and 1980, very few aliens invoked the ATS, and U.S. court jurisdiction was sustained through ATS only twice,<sup>150</sup> the *Filártiga v. Peña-Irala* opinion opened the judicial floodgates, and about 185 human rights cases have been filed, although the majority have been dismissed.<sup>151</sup> The most common reason for dismissal is a failure to prove that there was a violation of an actionable international norm.<sup>152</sup> Furthermore, the *Doe v. Unocal* decision introduced the notion of corporate liability, and it has been upheld by many cases since then. In fact, approximately 50 ATS cases have been filed against corporations since the *Unocal* decision.<sup>153</sup> Courts have consistently held in many of these cases that corporations can be held liable for human rights abuses under the ATS, although some have been dismissed on other grounds.<sup>154</sup>

Despite the large number of cases filed against corporations under the ATS, it is worth noting that these cases likely represent a small number of the actual human rights

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<sup>150</sup> Jennifer K. Elsea, "The Alien Tort Statute: Legislative History and Executive Branch Views," *CRS Report for Congress*, October 2, 2003, p. 11, <http://www.policyarchive.org/handle/10207/bitstreams/1864.pdf>.

<sup>151</sup> Stephens, "Judicial Deference and the Unreasonable Views of the Bush Administration," p. 777.

<sup>152</sup> Stephens, "Judicial Deference and the Unreasonable Views of the Bush Administration," p. 777.

<sup>153</sup> Stephens, "Judicial Deference and the Unreasonable Views of the Bush Administration," p. 773.

<sup>154</sup> Stephens, "Judicial Deference and the Unreasonable Views of the Bush Administration," p. 779.

abuses by corporations, and that there are some significant barriers to aliens successfully levying cases against transnational corporations. The first is the financial burden of litigating a case in the United States. Lawyers are expensive; consistently successful lawyers are often even more expensive. The legal fees involved in filing and maintaining a case against anyone is significant; added to this is the fact that these are transnational corporations which have the money to litigate each case to its ultimate conclusion, regardless of the number of appeals or the length of litigation. Because of this, many foreigners cannot file cases.

The financial issue raises another important and similar concern - the power imbalance between the two involved parties. The plaintiffs in these cases are often poor, rural and/or indigenous populations, while the defendants are mega-corporations with almost unlimited resources. This can be intimidating to potential plaintiffs in a case; the corporation may bully them into not filing at all, or settling for a small amount early in the proceedings.

Other smaller considerations include the distance between the plaintiffs' home and the difference in languages; these are other factors that may discourage or make it arduous to file and maintain cases in U.S. courts against any corporation. The final consideration is that the burden of proof of transgression lies with the plaintiffs. It is a daunting task to try to prove that a transgression happened when corporations can hire countless witnesses and investigators to "prove" that no transgression occurred.

All of these potential difficulties apply to the potential Alien Labor Statute. When considering the new law, there is also an additional difficulty for potential plaintiffs: the

need for employment. Most of the workers in these factories work to live; if they lose their jobs, they may not be able to survive. Even if it was made a condition of employment that filing a case against the commissioning corporation was not sufficient grounds for employment termination, many laborers may not feel secure enough to decide to file cases against the commissioning corporation.

These practical challenges underscore that it is necessary to construct this law so that it allows for class action lawsuits against a commissioning corporation. This will apply to both the workers in a single factory as well as the workers of several factories being commissioned by the same corporation. If workers can sufficiently prove that a corporation has been negligent in its monitoring of its factory or factories to the extent that hundreds or thousands of laborers live and work in conditions deemed illegal by the labors laws local to the factories, there is no reason that workers cannot, as a class, file a suit against said corporation. This approach will alleviate many of the aforementioned issues. As a class of hundreds or thousands, financial obligations become mitigated, the power imbalance becomes smaller, employment security becomes greater, and the burden of proof becomes easier to meet because the case becomes higher profile and there are more people available to gather proof. This certainly is not to say that individuals could not file a suit, but the availability of class-action suits is a must for this situation.

As with the tax incentive, it is important to consider the economic ramifications of the ALS. In order to do this, it must be determined what the penalties will be if the corporation is found liable for commissioning a factory which violates its local labor laws. It is necessary that the penalties be, at the minimum, the difference between the

wages paid and the minimum legal wages in each factory's region. This would include back-pay for any underpaid wages from the time of the passing of this law and the time of the decision, as well as the command to pay legal minimum wages into the future. Part of the penalties could also be a command to increase safety standards at each factory, if that it one of the illegal conditions named in the lawsuit. Punitive damages should only be issued in egregious cases, at the discretion of the judge and jury.

Given these guidelines, an estimation can be made of the average per-worker cost for a corporation found liable under the ALS. Revisiting the data presented in the tax Part One of this chapter, it can be found that the average difference between the minimum wage at each factory and the legal minimum wage for each factory's region is \$34.52 per worker per month. Data on the per-hour overtime wages does not exist for every factory and every region, making it difficult to estimate the per-worker cost of that standard. An earlier estimation of \$52.20 was made of the per-worker difference between the tax credit overtime wage and the factory minimum wage at 36 hours of overtime per month; this is an enormous overstatement of the average difference between the factory overtime wage and the regional minimum wage, but for the purposes of this thesis, it is the only possible estimation. It will be used for the purpose of calculating the average penalty given to a corporation in an ALS lawsuit, but accompanying it will be the understanding that it will be a significant overstatement. Finally, the estimation of the per-worker per-month cost of safety and infrastructure upgrades is \$25. It will be assumed that the example case involves a class-action lawsuit of 1000 workers at a single factory, and that it takes two years from the adoption of this law to reach a decision of corporate liability, and that the

corporation takes no steps to better the workers' conditions in those two years. Based on the averages above, the backpay owed to each worker is \$2081.28. Assuming that there are no punitive damages, for 1000 workers, that comes out to \$2,081,280 in damages. It is important to remember that this is a vast overstatement of the average cost.

This amount does not reflect the costs incurred by the corporation given the court demands to increase wages and safety moving forward. Again, using the averages determined above, those costs come out to \$111.72 per worker per month. At 1000 workers, this per-month cost to comply with local labor laws is \$111,720 for the first year, and \$86,720 for each year after that. Again, these are overestimations, but it is important to analyze the potential economic cost of such a policy.

From these numbers it can be shown that the penalty from the actual court decision as well as the first year of increased production cost adds up to \$3,421,920 for a corporation which commissions a single factory which employs 1000 workers. This number will scale upward for corporations which commission more factories with more workers. This would be a significant financial impact on a corporation which would likely have significant impacts on the overall economy. This is especially true if, as predicted, more workers gain the confidence to file claims against corporations as class-action lawsuits. One way for corporations to mitigate these costs or eliminate the possibility of legal action is to pursue the tax credit outlined in Part One. Pursuit of the tax credit, however, should not be the only means by which a corporation can protect itself. It is necessary, then, to outline a legitimate defense for a corporation against a claim under the ALS.

In his law review article, “Due Diligence as a Defense to Corporate Liability Pursuant to the Alien Tort Statute,” scholar Lucien Dhooge considers the benefits of a due diligence defense to the ATS. As part of his formulation of the due diligence defense, Dhooge uses the business judgment rule, which provides that “the business judgment of the directors will not be challenged or overturned by courts or shareholders, and the directors will not be held liable for the consequences of their exercise of business judgment - even for the judgments that appear to have been clear mistakes.”<sup>155</sup> Dhooge goes on to say that this rule “creates a presumption that in making the decisions in questions, the directors ‘acted on an informed basis in good faith and in the honest belief that the action was taken in the best interests of the company.’”<sup>156</sup> This conception of due diligence has tremendous relevance in relation to the proposed ALS. If corporation practices due diligence in their monitoring of factories, if they are not negligent, then this should be a defense to legal claims filed against them under the parallel ATS law. So, rewording Dhooge’s concept for the purposes of the ALS, the director of a corporation should, in making decisions about the treatment of factory workers, act on an informed basis in good faith and in the honest belief that the action was taken in the best interests of the company and the factory workers. The question arises: how does the director act on an informed basis in good faith? It would be the director’s responsibility to ensure that a reasonable job is being done to monitor factories. The interpretation of reasonable may be up to the courts, but a fair interpretation might be that the director issued bi-annual audits

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<sup>155</sup> Lucien J. Dhooge, “Due Diligence as a Defense to Corporate Liability Pursuant to the Alien Tort Statute,” *Emory International Law Review*, Volume 22, Issue 2 (2008), pp. 476-477, accessed March 9, 2012, <http://www.law.emory.edu/fileadmin/journals/eilr/22/22.2/Dhooge.pdf>.

<sup>156</sup> Dhooge, “Due Diligence as a Defense to Corporate Liability Pursuant to the Alien Tort Statute,” p. 477.

of the factory that included interviews with factory workers and an inspection of safety standards. If these standards, which are not much more stringent than current corporate monitoring practices, are met, then the corporation should have due diligence as a defense to any suit filed by workers. The corporation can only do so much to prevent deceit from factories; if workers are willing to lie to auditors about working and living conditions, then they should not be permitted to sue the commissioning corporation later for noncompliance. Of course, truth-telling and whistle-blowing should be made insufficient grounds for employment termination in every factory.

The corporate due diligence defense has some serious benefits. For one, it can significantly reduce the financial burden on corporations which might otherwise be found liable under the ALS. As Dhooge points out, “recognition of a due diligence defense would result in transnational corporations incurring costs to ‘alter their decisions about location, timing, design, and costing, and thus the investment’s overall viability, based on the impact assessment.’ Corporations would incur these costs earlier than litigation costs, and they would be significantly smaller.”<sup>157</sup> Slightly modified to more directly apply to the factories instead of human rights abuses, this means that the recognition of a due diligence defense would result in transnational corporations incurring costs to reasonably monitor factories and factory worker conditions.

Given these considerations, it seems that a tax credit and the adoption of a parallel law to the Alien Tort Statute - to be known as the Alien Labor Statute - would be extremely effective means of combating labor abuses in countries with inadequate and/or

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<sup>157</sup> Dhooge, “Due Diligence as a Defense to Corporate Liability Pursuant to the Alien Tort Statute,” p. 488.



poorly enforced labor laws. The tax credit gives a large incentive to corporations to ensure that their factories' workers are being treated adequately, by making it profitable for them to do so. The ALS gives foreign workers a means to pursue legal action against corporations which commission factories which violate foreign labor laws. The due diligence defense for corporations makes it easy for corporations to avoid costly liability through the reasonable monitoring of their factories, thus eliminating any disastrous economic concerns.

## **Chapter IV: Criticisms and Impact Analysis**

Plans which attempt to overturn decades of status quo, no matter how feasible, are often met with significant criticism. It is always the job of those who propose such plans to answer potential criticisms to the best of their abilities. The proposed tax credit and Alien Labor Statute constitute such a controversial plan, and this chapter will be dedicated to answering potential criticisms and projecting the impacts that the new policies will have. The addressed criticisms range from commentary on the effectiveness of monitoring and non-local organizations to proposals of alternative plans to predictions of international relations nightmares.

### **Part One: The Effectiveness of Monitoring**

In the study “Does Monitoring Improve Labor Standards? Lessons From Nike,” researchers Richard Locke, Fei Qin, and Alberto Brause use data on factory audits of working conditions in over 800 of Nike’s suppliers over the years of 1998-2005 to analyze the effectiveness of Nike’s monitoring policies.<sup>158</sup> After providing background

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<sup>158</sup> Richard Locke, Fei Qin, and Alberto Brause, “Does Monitoring Improve Labor Standards? Lessons From Nike,” Working Paper No. 24 of the Corporate Social Responsibility Initiative (July 2006), Harvard University, pp. 9-14, accessed March 16, 2012, [http://www.hks.harvard.edu/m-rcbg/CSRI/publications/workingpaper\\_24\\_locke.pdf](http://www.hks.harvard.edu/m-rcbg/CSRI/publications/workingpaper_24_locke.pdf).

information about Nike and the athletic shoe industry, Locke outlines the three types of monitoring done on Nike Factories: the SHAPE inspection, launched in 1997, is done by Nike's field-based production staff once or twice a year, and provides a "very general picture of the factory's compliance with labor, environment, safety and health standards"; the M-Audit (Management Audit), launched in 2002, is conducted by Nike's in-house compliance specialists, takes several days to complete and is announced beforehand, and is seen as the core of Nike's compliance program, as it is the most rigorous of Nike's audits; finally, there is also independent monitoring by the Fair Labor Association, which is conducted on about 5% of Nike suppliers every year and are unannounced.<sup>159</sup>

Through the analysis of the data, Locke finds that despite the fact that Nike has "significantly expanded its compliance staff, invested heavily in the training of its staff and that of its suppliers, developed ever-more rigorous audit protocols and internalized much of the auditing process, worked with third party social auditing companies and NGOs to check its own internal audits, and spent millions of dollars to improve working conditions at supplier factories," monitoring by itself "appears to produce limited, and perhaps only mixed results."<sup>160</sup>

This criticism is a real concern for the proposed tax credit, since the enforcement and benefits of the credit relies exclusively on effective monitoring. Not only that, but the improved monitoring methods employed by Nike appear, at first glance, to be identical to

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<sup>159</sup> Richard Locke, Fei Qin, and Alberto Brause, "Does Monitoring Improve Labor Standards? Lessons From Nike," p. 13.

<sup>160</sup> Richard Locke, Fei Qin, and Alberto Brause, "Does Monitoring Improve Labor Standards? Lessons From Nike," pp. 27, 35.

the measures suggested in this paper. There are differences, though, and it is in those differences that the tax credit will be more effective than Nike's monitoring practices.

The most significant difference is that the tax credit monitoring improvements involve more parties which have something to gain from improved labor conditions. Factories have nothing to lose, because they are passing the costs along to the commissioning corporations. Corporations have plenty to gain because they are the recipients of the tax credit which will increase their profits. More than that, corporations could advertise the fact that they qualify for the tax credit. In an era where corporate responsibility matters to consumers, companies can wear this tax credit as a badge of honor. Then the companies are not only receiving compensation from the government in the form of the tax credit, they are also increasing business through a positive public image. Most important, the Chinese administrators who conduct the official audits have much to gain because increased labor conditions boost the local economies, which reflect well on the management policies of the local leaders. Creating a situation in which all involved parties benefit will substantially increase the effectiveness of monitoring in a way that Nike could not.

## **Part Two: Local or International Watchdogs?**

An argument related to Locke's criticism of monitoring comes from Amy Westervelt, a contributor for Forbes. In an article she wrote in December of 2011, she outlines several examples in which small, local Chinese NGOs were more effective at monitoring factories than larger, American NGOs or the corporations which

commissioned the factory. She writes, “Chinese companies today are less cowed by the threat of a massive Greenpeace campaign. Instead it is the work of small, local NGOs and watchdog groups bringing labor infractions to light.”<sup>161</sup> She goes on to suggest some reasons which might explain the effectiveness of local organizations over Western ones: “Because these local groups can more easily infiltrate factories, and because they are not open to accusations of imposing Western ideals on Chinese work culture, their investigative work may be far more effective than that of their Western counterparts when it comes to shifting the way China does business.”<sup>162</sup>

There are two responses to these claims with regard to the proposed tax credit and ALS. The first is that Westervelt is partially correct. Local organizations are more effective at monitoring. Most organizations must have local buy in to be effective. Where she is wrong is in her insinuation that Westerners play a small role in combating labor abuse in overseas factories. China Labor Watch, a major NGO in the field of labor rights, is an international organization that has offices in both China and the United States. The two offices work together to put together their reports, which have been extremely effective in effecting change in corporate policy. Westervelt is correct in saying that organizations that have no presence in countries in which they are investigating will find it difficult to produce effective results; a blonde American woman will not likely be able to infiltrate a factory as a local Chinese worker. But Westerners and locals can work

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<sup>161</sup> Amy Westervelt, “How Local Watchdog Groups, Not Western Companies, Are Shaping Business Practices in China,” *Forbes*, December 06, 2011, accessed March 5, 2012, <http://www.forbes.com/sites/amywestervelt/2011/12/06/how-local-watchdog-groups-not-western-companies-are-shaping-business-practices-in-china/>.

<sup>162</sup> Westervelt, “How Local Watchdog Groups, Not Western Companies, Are Shaping Business Practices in China.”

together, which will often produce the most effective results. The Chinese branch of China Labor Watch “works closely with local factories and services migrant workers in Guangdong through free Legal Consulting Hotline Program, Community Training in collective bargaining, and Train the Trainer Program to enhance the local capacity in labor movements.”<sup>163</sup> It is doing exactly what Westervelt says it is able to do: it infiltrates factories and understands Chinese work culture. The U.S. Branch also plays a vital role, as it “creates reports from these investigations, educates the international community on supply chain issues, and pressures corporations to improve conditions for workers.”<sup>164</sup> Effecting change from the corporate perspective also takes cultural knowledge in which Westerners are much more versed. Westervelt herself shows that the local Chinese organizations which conducted factory investigations and had no American branch had to rely on American news organizations to spread their message and pressure American corporations.<sup>165</sup> There is clearly room for both cultures to work together to effect change, and this combination of effort is exactly what the monitoring improvements for the tax credit accomplishes.

The second answer to Westervelt’s criticism is similar to the answer to Locke’s commentary: the tax credit creates a system in which all involved parties will benefit from effective monitoring and improved work conditions. Such a system will be much more successful in ensuring that changes are made and that work conditions improve.

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<sup>163</sup> “Who We Are,” *China Labor Watch*, accessed March 16, 2012, <http://www.chinalaborwatch.org/aboutus.html>.

<sup>164</sup> “Who We Are.”

<sup>165</sup> Westervelt, “How Local Watchdog Groups, Not Western Companies, Are Shaping Business Practices in China.”

### **Part Three: Consumer Mobilization vs. Policy Change**

In the study “Mobilizing Consumers to Take Responsibility for Global Social Justice,” authors Michele Micheletti and Dietlind Stolle suggest that the most effective means of combatting “sweatshops” is the mobilization of consumers.<sup>166</sup> One of the first things that the authors do is indict the government for not taking enough responsibility for factory labor abuse: “Government inaction on global social justice responsibility [...] shows that existing political institutions charged with caring for the world are not proving that they can successfully take responsibility for global problems.”<sup>167</sup> They go on to say that, “traditional government political responsibility, which is premised on the existence of state authority (jurisdiction) for problem solving and identifiable actors that can be made legally accountable for their specific actions, are ill suited to take charge of solving pressing complex global problems.”<sup>168</sup> The authors conclude, “Even if good laws are in place, governments in developing countries for different reasons may not have the capability or willingness to prosecute transnational garment corporations for wrongdoings. And without good laws, it is not even possible to hold wrongdoers legally accountable for their actions.”<sup>169</sup>

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<sup>166</sup> Michele Micheletti and Dietlind Stolle, “Mobilizing Consumers to Take Responsibility for Global Social Justice,” *Annals of the American Academy of Political and Social Science*, Vol. 611, *The Politics of Consumption/The Consumption of Politics* (May, 2007), pp. 157-175, accessed March 16, 2012, <http://www.jstor.org/stable/25097915>.

<sup>167</sup> “Mobilizing Consumers to Take Responsibility for Global Social Justice,” p. 159.

<sup>168</sup> “Mobilizing Consumers to Take Responsibility for Global Social Justice,” p. 159.

<sup>169</sup> “Mobilizing Consumers to Take Responsibility for Global Social Justice,” p. 159.

The authors discuss why customer mobilization is effective in changing corporate behavior. They identify four distinct consumer roles: “(1) support group for a broader cause, (2) critical mass of fair trade shoppers, (3) “spearhead force” of corporate change, (4) ontological agent of social change.”<sup>170</sup> After outlining each of these, the authors explain that “no matter what the consumer role, the movement uses two types of frames, episodic and thematic, to get consumers to see and act on the connections between their apparel choices and the realities of outsourced manufacturing for garment workers.”<sup>171</sup> Episodic frames, which “focus on particular issues and put responsibility claims on specific wrongdoers,” are the more frequently used of the two:

“Not surprisingly given the consumer roles characteristic of much of the movement, most antisweatshop mobilizing activism stresses episodic campaigning and focuses on high-profile specific events because [...] ‘It is by taking action in our everyday lives, by provoking consumers to question what they are buying and as they buy, that we will move forward.’ Antisweatshop movement actors believe that episodic consumer campaigning can convince corporations to accept unions and collective bargaining, improve their codes of conduct, allow for third-party monitoring of their implementation, and in the end, help alleviate social injustices in the global garment industry.”<sup>172</sup>

The authors then consider some of the real-world impacts of consumer mobilization: “With the metaphor “sweatshop” as its common master frame, the movement has been able to communicate complex information in an easily understandable way. It has even developed innovative resources to convince consumers, journalists, civil society, and governments that sweatshop problems demand new models

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<sup>170</sup> “Mobilizing Consumers to Take Responsibility for Global Social Justice,” p. 166.

<sup>171</sup> “Mobilizing Consumers to Take Responsibility for Global Social Justice,” p. 168.

<sup>172</sup> “Mobilizing Consumers to Take Responsibility for Global Social Justice,” p. 168.



of responsibility-taking.”<sup>173</sup> Furthermore, the word “sweatshop” has “entered consumer thinking, as witnessed by the global resonance of the Nike Email Exchange, a culture jam that used the sweatshop to toy with Nike’s marketing image and, in doing so, made national and international news.”<sup>174</sup> Finally, the authors point out that

“Ongoing research finds that corporations are developing more antisweatshop friendly policies and practices. The movement has been able to force reluctant and formerly blame-avoiding corporations to take social justice responsibility and adopt codes of conduct. A good case in point is Nike, which after years of sustained antisweatshop criticism improved its code of conduct, issued its first Corporate Responsibility Report, opened to independent monitoring, disclosed its outsourced factory locations, increased minimum wage requirements, and improved health and safety conditions.”<sup>175</sup>

The authors conclude that “antisweatshop activism has bite - even if change comes slowly, unevenly, very incrementally, and if doubt still exists about [...] corporations’ dedication to social justice responsibility-taking. The question is how sharp antisweatshop’s teeth are and how big of a bite it really can make into corporations.”<sup>176</sup> The response to this alternative plan begins with its conclusion - antisweatshop consumer mobilization will take far too long to gain enough traction to make a big dent in factory labor abuse, if it can even truly fix the problem at all.

The problem really lies in the authors’ own example of the movement’s impact: Nike may have done all it could to take social justice responsibility, but as the earlier study pointed out, its improved monitoring techniques were ultimately ineffective at

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<sup>173</sup> “Mobilizing Consumers to Take Responsibility for Global Social Justice,” p. 171.

<sup>174</sup> “Mobilizing Consumers to Take Responsibility for Global Social Justice,” p. 171.

<sup>175</sup> “Mobilizing Consumers to Take Responsibility for Global Social Justice,” p. 172.

<sup>176</sup> “Mobilizing Consumers to Take Responsibility for Global Social Justice,” p. 172.

actually bettering factory workers' conditions. This shows that while consumer mobilization may have some superficial effect on corporate responsibility-taking, it is unlikely that it will ever be as effective as the proposed tax credit and Alien Labor Statute, which create a situation that encourages all parties to improve labor standards. That is the path to truly effecting change.

The authors are correct in their initial criticism of national governments; too little has been done to take responsibility for improving the living and working conditions of overseas factory laborers. This does not mean, however, that governments cannot change their stance on the issue and begin to take such responsibility. In fact, this is exactly what this paper is encouraging - that the United States and local governments should take charge of the situation, and create a system which incentivizes the relevant parties to change their ways of doing business. There is also an answer to the authors' prediction that "governments in developing countries for different reasons may not have the capability or willingness to prosecute [...] corporations for wrongdoing."<sup>177</sup> While not all of the different reasons for such a situation can be addressed here, some of the major reasons can. The biggest barrier is that of training and effectiveness, which has already been addressed in Chapter III. With the proper training from watchdog groups and NGOs, local officials will find it much easier to monitor effectively. There is also the fact that the tax credit will reduce the need for government monitoring by increasing the incentive for effective self-monitoring. The argument that the local governments may not be willing to

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<sup>177</sup> "Mobilizing Consumers to Take Responsibility for Global Social Justice," p. 159.

help has also already been addressed: the system created by the tax credit makes it beneficial to local officials to participate and help with effective monitoring.

#### **Part Four: Americans Subsidizing Chinese Workers' Wages**

The final major criticism is a practical side effect of the proposed tax credit: American taxpayers will be subsidizing the improved wages and working conditions of Chinese factory workers. This is after the multinational corporations already outsourced American factory jobs to China in the first place. Many would view this as simply adding insult to injury. While nothing can be done to change the reality that American tax dollars will be paying corporations to improve factory wages and conditions, there are practical side effects of the better labor standards that may benefit American workers in the long run.

Economist Christian E. Weller used trade data from 2001 to 2007 to analyze the effect of improved labor conditions on the United States economy. Weller found that “US exports would have been about three times as large if incomes and relative export prices in countries with weak or no worker rights had been similar to incomes and relative export prices in countries with some or strong worker rights.”<sup>178</sup> Furthermore, not only would U.S. Exports have been tripled, but “US imports would have largely remained unchanged” if the labor rights had been improved.<sup>179</sup> His conclusion from the analysis of this data is that the United States trade deficit would “have been substantially smaller

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<sup>178</sup> Christian E. Weller, “Could International Labour Rights Play a Role in US Trade?,” *Cambridge Journal of Economics*, May 26, 2010, p. 54, accessed March 18, 2012, doi:10.1093/cje/beq011.

<sup>179</sup> Weller, “Could International Labour Rights Play a Role in US Trade?” p. 54.

than it was in reality if all US trading partner countries had some or strong labor rights between 2000 and 2007.”<sup>180</sup>

Weller goes on to recommend that future trade agreements in the United States should include provisions on labor standards, because “the proliferation of better worker rights abroad thus could result in more balanced US trade.”<sup>181</sup> While making labor rights a priority in future trade agreements may increase labor rights in some countries, the proposed tax credit and Alien Labor Statute are immediate solutions for all countries with factories. Those two policy changes will manifest the same increase in U.S. exports that Weller predicts. So, while U.S. taxpayers may have to subsidize the improvements in Chinese factory wages and standards for the first year or two, the better working conditions would quickly begin to pay for themselves through lower U.S. trade deficits. This boost to the U.S. economy would outweigh any negative impact of reallocating tax dollars to corporations. More than this, the better U.S. economy would help to soothe the negative sentiments of Americans who feel they should not be subsidizing Chinese factory condition improvements; in reality, they would be subsidizing a smaller U.S. trade deficit.

Furthermore, while the first prong of this approach, the tax credit, does use U.S. tax dollars to subsidize improved wages and safety conditions overseas, the second prong of the approach, the Alien Labor Statute, may help bring jobs back to the United States. Boston Consulting Group has done both a study and a survey about the growing trend of reshoring manufacturing jobs - that is, bringing manufacturing jobs back to the United

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<sup>180</sup> Weller, “Could International Labour Rights Play a Role in US Trade?” p. 56.

<sup>181</sup> Weller, “Could International Labour Rights Play a Role in US Trade?” p. 56.

States. The original study, done back in March of 2012, found that the low wages, one of many incentives that drove many manufacturing jobs to China and other unindustrialized nations in the first place, are not so low anymore.<sup>182</sup> The rising wages, according to BCG, will play a significant role in the reshoring of manufacturing jobs in the relatively near future. A survey released on April 20, 2012, found that “more than a third of U.S.-based manufacturers executives at companies with sales greater than \$1 billion are planning to bring back production to the United States from China or are considering it.”<sup>183</sup> More than half of those executives who answered affirmatively cited labor costs as a top factor driving future decisions.<sup>184</sup> This survey only reinforced BCG’s initial prediction - the United States should be getting some of its manufacturing jobs back soon.

It is clear that minimum wage regulations, like those in China’s Labor Law, are driving up the cost of manufacturing, even when those laws are not rigorously enforced (as has already been demonstrated). With the advent of the Alien Labor Statute, it will be even easier to ensure that such regulations are enforced, making the cost of production in foreign countries even less cost-effective. It can be presumed, then, that such a law would quicken the pace of manufacturing job reshoring, thereby alleviating some of the anger and indignation of American tax-payers.

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<sup>182</sup> Harold L. Sirkin, Michael Zinser, Douglas Hohner, and Justin Rose, “U.S. Manufacturing Nears the Tipping Point,” Boston Consulting Group, March 22, 2012, [https://www.bcgperspectives.com/content/articles/manufacturing\\_supply\\_chain\\_management\\_us\\_manufacturing\\_nears\\_the\\_tipping\\_point/#chapter1](https://www.bcgperspectives.com/content/articles/manufacturing_supply_chain_management_us_manufacturing_nears_the_tipping_point/#chapter1).

<sup>183</sup> “More Than a Third of Large Manufacturers Are Considering Reshoring from China to the U.S.” Boston Consulting Group, April 20, 2012, <http://www.bcg.com/media/PressReleaseDetails.aspx?id=tc:12-104216>.

<sup>184</sup> “More Than a Third of Large Manufacturers Are Considering Reshoring from China to the U.S.”

These criticisms reflect significant potential problems for the proposed policy changes, and they shed light on some of the plan's weaknesses. The answers to these criticisms illustrate the intricacies of the plan, and demonstrate that through these intricacies it is insulated from the stated concerns. Most important, this investigation has reaffirmed the fact that these policy changes are not only feasible, but that they will be effective at improving factory worker conditions.

## **Conclusion**

Factory labor abuse is a global concern that deserves international cooperation to remedy. China has provided blatant examples of labor abuse in factories which supply major U.S. companies. The corporations have yet to implement effective solutions to these labor abuses, and consumer mobilization is also not a viable alternative to the severe problems in the status quo. There are, however, existing U.S. laws that are ripe for modification.

The proposed tax credit, awarded for compliance with high standards of working conditions, creates a monitoring system unique in its maintenance of multifaceted global social justice responsibility. All major stakeholders play a role in the monitoring, and all maintain a certain level of culpability in the system. Most important, the monitoring system is one which benefits all involved parties, greatly increasing its chances of success at fundamentally improving working conditions in factories.

The Alien Labor Statute, modeled after the Alien Tort Statute, provides factory workers with the legal recourse for tortuous corporate behavior in the enforcement of local labor laws. A vital feature of this legal recourse is the availability of class action lawsuits, which mitigate many of the barriers that face foreigners when filing a suit

against a transnational corporation in American courts. The recognition of the defense of due diligence for corporations will curb potential abuse of the ALS, and provide corporations with a means to soften the financial impact of losing an ALS suit.

When combined, these two policy changes represent a multi-pronged approach to the problem of factory labor abuse. They incentivize stakeholders to effect real change, something that previous approaches have failed to do. Most important, these policy changes represent effective solutions that come with small and justifiable costs. Both plans are crafted carefully to help avoid fatal economic and enforcement hitches.

These two policy changes ought to be enacted immediately. Each plan represents values and accomplishes goals that appeal to both ends of the political spectrum. Neither plan represents a significant departure from existing statutes or common law. There are few real barriers to the implementation of both of these policy changes. There are very few negative impacts. Yet there is so much to gain.