

MIMCO

**Mattel Independent Monitoring Council for
Global Manufacturing Principles**

Follow –up audit report

For

Guan Yao (Zhongmei) Plant

And

Chang An (Meitai) Plant

November 1, 2000

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September 9, 2000

INTRODUCTION

This report is based on the results of a follow-up audit that was conducted to verify issues pertaining to the two Mattel China plants, i.e., Guan Yao (Zhongmei) plant, and Chang An (Meitai) plant. The first audit of these two plants took place in March 1999 and was reported in the MIMCO Global Manufacturing Principles (GMP) audit report published in November 1999.

A major issue during the first audit pertained to the system of keeping payroll data, including regular and overtime hours, breakdown of wages paid, performance bonuses, and the transmittal of this information to the employees through pay stubs. The system then used by the two plants was found, in the opinion of MIMCO, to be complex and difficult to comprehend. Consequently, MIMCO, Mattel and the management of the two plants, agreed to postpone this portion of the audit to enable the two plants to redesign their payroll systems and to make them simpler and more transparent to employees.

Mattel and the management of the two plants have developed a new payroll system structure (Exhibit 1) and a paystub (Exhibit 2). MIMCO and its financial auditors find the new payroll data management system to be satisfactory. It is proposed by MIMCO that the new system be adopted in all of Mattel's plants and its vendor plants in China. After a lengthy period of trial runs, the new system became fully operational in May 2000.

This follow-up audit was conducted on June 19-20, 2000. It covered all outstanding issues pertaining to the operations of the two plants that were raised in the first report.

GUAN YAO (ZHONGMEI) PLANT

Overall Conclusion

Our follow-up audit revealed that the Guan Yao plant's management had made a good faith effort, and achieved remarkable success, in addressing all of the issues of concern expressed by MIMCO in its first audit report. We believe that both Mattel and its China partners can take satisfaction in the quality of maintenance of their plant facilities, employees' living and working conditions, and a friendly work environment. With two exceptions, as noted below, the Guan Yao plant has met Mattel's GMP standards. We commend both Mattel and the Guan Yao team for this progress.

Calculation of working hours and wages

Guan Yao pays its employees on a piece-rate system. However, for our purposes, we calculated wages on the basis of minimum wages per month mandated by the government in this area. A similar rationale was used in calculating wages for overtime hours. Our audit of the payroll data showed that Guan Yao plant's employees uniformly received wages that exceeded the minimum mandated wages for regular working hours (RMB 430 per month). The only exception is that The normal working week (including overtime) at Guan Yao is 60 hours. This is in excess of the maximum

hours per week prescribed in the Chinese Labor Law, which consist of 40 hours of regular time, no more than 3 hours of overtime per day with a maximum of 36 overtime hours per month.

Our analysis of benchmark data available for this area, however, shows that with rare exception, most plants in the area operate at rates that exceed the maximum number of hours allowed by the Chinese Labor Law. Mattel requires that these plants receive dispensation from the local labor bureau. Guan Yao has obtained this specific approval to work the 60-hour weekly schedule. However, MIMCO notes that this dispensation does not conform to the letter of the law.

Maternity Leave

The Chinese Labor Law provides for 90 days of paid maternity leave for all employees. In MIMCO's previous audit report, it was noted that Guan Yao provided maternity leave only to management staff. Production employees were not granted any maternity leave, which was not in compliance with the Chinese Labor Law.

The follow-up audit showed that Guan Yao has made an improvement (effective January 1, 2000) in this policy by providing one month paid maternity leave to all employees who had completed three years of full service. MIMCO found this to be unsatisfactory since most line employees have average tenure of less than three years. Consequently, the management of the Guan Yao plant has agreed to implement a maternity leave program that fully complies with the Chinese labor law. MIMCO will follow-up on this question within 90 days to ensure that proper implementation procedures have been put in place.

Work Environment

The plant has installed a new ventilation system and upgraded ventilation in the spray painting operation including additional exhaust fans, thus improving air quality in the spray painting, hot melt glue and solvent bonding areas. The plant air is regularly monitored and air quality meets GMP standards. MIMCO examined the plant's employee monitoring data which verified that it was in compliance with the Chinese regulations and those of the Mattel GMP.

Dormitory Space

With the renovation of two old dormitories and building of two new dormitories, Guan Yao has made significant progress in further increasing space for employees. Each employee is provided with lockable storage for personal items. All four dormitories now meet or exceed GMP standard for minimum living space per employee.

The building of new dormitory space has also permitted the plant management to significantly enhance floor area devoted to recreational facilities. A new canteen with an area of 38,000-sq. ft. in Dormitory # 4 is scheduled to open in October 2000.

On-Site Medical Facilities and Maintenance of Employee Injury Records

The on-site medical facility is scheduled for completion in October 2000. Following MIMCO's recommendation, Guan Yao plant now maintains detailed employee injury data and other pertinent medical records. Our analysis showed that Guan Yao's employee injury rates for various categories of work-related injuries were below the rates allowed in GMP.

Enhanced Employee Communications and Awareness of GMP

The plant has initiated an enhanced employee orientation program that emphasized greater awareness of GMP. Programs for job-related new employee training have also been strengthened and proper records maintained with regard to the training regime for various job categories, number of employees trained, etc.

For the first time, the top manager of the Guan Yao Plant has initiated open gatherings where senior plant executives meet with employees in small groups to discuss issues of concern to employees. This is an encouraging start. We earnestly hope that the management will continue to take additional steps in building greater channels of communications between employees and different levels of management.

Chang An (MEITAI) Plant

Overall Conclusion

Our follow-up audit revealed that the Chang An Plant's management had made significant effort in addressing various issues of concern expressed by MIMCO in its first

audit report. We believe that both Mattel and its China partner can derive ample satisfaction for its plant facilities, employees' living and working conditions, and a friendly work environment. With two exceptions, as noted below, Chang An plant has satisfactorily met Mattel's GMP standards. We commend both Mattel and Chang An for this progress. The unresolved issues, in our opinion, are minor and should be easily handled in the foreseeable future given goodwill on the part of all concerned. We plan to monitor Mattel's progress in resolving those issues with its China partner.

Calculation of working hours and Wages

Chang An pays its employees on a piece-rate system. However, for our purposes, we calculated wages on the basis of minimum wages per month mandated by the government in this area. A similar rationale was used to calculate wages for overtime hours. Our audit of the payroll data showed that Chang An plant's employees uniformly received wages that were in excess of the minimum mandated wages for regular working hours (RMB 400 per month).

The normal working week (including overtime) at Chang An is 60 hours. This is in excess of the maximum hours per week prescribed in the Chinese Labor Law, which consists of 40 hours of regular time, no more than 3 hours of overtime per day with a maximum of 36 hours per month.

Our examination of the payroll data also showed that in the case of the Injection Molding Department, which represents approximately 500 employees or 7% of the workforce was working in excess of the 60-hour limit. The average hours worked in the sample examined was 63 hours per week. It would appear that Mattel's managers were

unaware of this practice and had not concurred with it. Immediately upon learning of this irregularity, Mattel management committed to returning the molding area employees to a schedule of 60 hours per week. Our follow-up inquiries have confirmed the fact that the molding area employees are now following the 60-hour/week schedule. The plant's line supervisors have been counseled on the working hour requirement and the payroll department has been alerted to notify management immediately if any employee has been required to work beyond the 60-hour per week limit.

With regard to 60-hour work-week, our analysis of benchmark data available for this area, however, shows that with rare exception, most plants in the area operate at rates that exceed the maximum number of hours allowed by the Chinese Labor Law. Mattel requires that these plants receive dispensation from the local labor bureau and the Chang An plant has obtained specific approval for working 60 hours. However, as is the case with the Guan Yao plant, MIMCO notes that this dispensation does not conform to the letter of the law.

Maternity Leave

The Chinese Labor Law provides for three-months of paid maternity leave for employees. In MIMCO's previous audit report, it was noted that Chang An employees were not given any maternity leave. The follow-up indicated that the Chang An management has instituted a new maternity leave policy starting in January 2000. The new policy provides for 45-day paid maternity leave to salaried staff with similar benefits extended to production employees starting in 2001.

Following discussions with Mattel management it was decided that they will require Chang An to implement 90 days of maternity for all employees effective January 1, 2001.

Paid Annual Leave

Chang An has also initiated a policy of “paid annual leave”. Starting in 2001, all salaried staff will be entitled to five-days of paid annual leave. This benefit will be extended to production workers in 2002.

Work Environment

Chang An management has undertaken a number of actions to improve the ventilation system in the plant. These include: installation of evaporative air conditioning system, fresh air duct system, and additional exhaust fans. The new systems have improved air quality in areas containing hot melt glue, solvent bonding, and spray painting. The plant air is regularly monitored and air quality meets Mattel standards. The plant provided the MIMCO audit team (which verified compliance) with the Chinese Law regulations and Mattel’s GMP standards.