

Complaint – Haglöfs Scandinavia AB, KTC Limited – China

Status: Completed

FWF is responsible for setting up a complaints procedure in production countries where FWF is active. The complaints procedure allows third parties to make complaints about the working conditions or the way the Code of Labour Practices is implemented in factories which supply FWF members.

The responsibility of FWF includes investigating the complaint, verifying whether the agreed corrective action plan is implemented and public reporting. This complaint report gives an overview of a complaint filed to FWF, the investigation and agreed corrective action plan as well as how the outcome is verified. For more information on the complaints procedure see the FWF website. FWF also publishes an overview of complaints received in its annual reports.

1. Member company involved

Haglöfs Scandinavia AB, KTC Limited.

2. Accused party

Haglöfs Scandinavia AB.

3. Date of receiving complaint

October 23, 2015.

4. Filing party

Management of KTC Limited.

5. The complaint

The complainant, KTC Limited (KTC), claimed that Haglöfs Scandinavia AB (Haglöfs) failed to provide enough advance notice of its intention to cancel production. The complainant claims that this late order cancellation left a significant gap in production that is very difficult to fill. This production gap left KTC unable to work towards better compliance with FWF's Code of Labour Practices and could necessitate lay-offs of workers.

6. Admissibility

FWF decided that the case is admissible on October 23, 2015.

KTC Limited is an active supplier of Haglöfs, both members of FWF.

The case is relevant to the labour standards of FWF's Code of Labour Practices, as the complainant indicates that Haglöfs' decision hampered its ability to work towards better compliance to FWF's Code of Labour Practices.

7. Investigation

FWF informed Haglöfs about the case on November 5, 2015. Haglöfs responded to the complaint on November 11, 2015. Because the case focuses on the purchasing practices of one of FWF's member brands with in relation to one of FWF's factory members, FWF decided to seek the input of an independent garment industry expert for assistance in the analysis of the complaint.

This independent expert studied the documentation provided by both parties and provided a list of additional questions to each party. Both parties responded to the request for additional information on a timely basis. Based on this information, the independent garment industry expert provided an analysis of the complaint found below, determined culpability and provided recommendations.

8. Findings and conclusions

Haglöfs and KTC have worked together for more than 10 years. During this time, the size of the contracted business together grew to reach a high point in 2014. However, this was not sustained and the business between the parties declined during 2015. It would appear from the submissions from both parties that the reasons for this decline were explained, understood and accepted by both sides.

What also appears to not be in any dispute in the information provided is that:

- On May 29th 2015: Haglöfs placed their SMS order to KTC and also provided indicative dates for their FW2016 production forecast, which they expected to be placed in September 2015.
- KTC were only being asked to produce samples for 4 carry-over styles.
- On September 18th 2015: KTC shipped the FW2016 SMS samples to Haglöfs.
- On September 22nd 2015: Haglöfs advised KTC that they would be getting no production orders for the FW2016 collection.

KTC claim that this notification came as a surprise to them and left them with less than 2 months' notice to replace the expected production from Haglöfs. Furthermore, it appears that Haglöfs did not seek to enquire as to whether this would lead to any layoffs, or have any other major implications for KTC before making their decision. KTC have said that they understand that brands may re-source business to other factories but that to do this at such a late time in the product cycle was 'unethical' on the part of Haglöfs. In support of their claim, KTC also cite what they regard as a similar situation which occurred with Haglöfs for a product that they developed for Haglöfs for an earlier Spring/Summer collection. KTC say that this was re-sourced by Haglöfs for price reasons – but only after the forecast production had been provided to KTC by Haglöfs.

Haglöfs, in response to the complaint by KTC, stated that several times during ‘the last years’ their Sourcing Manager had made complaints to KTC that the cooperation with KTC was not working properly and that the product planning schedule and deliveries were late. They also had complaints about a lack of flexibility and production planning, etc. They further indicated that this was once again communicated verbally to KTC at the OurDoor Show in Friedrichshafen in July 2015. Haglöfs state that in their email to KTC on 22nd September they explained that they had been through a process of rationalizing their supplier base with the aim of reducing their number of suppliers by 50% and to give more of their production to fewer suppliers. They also advised that as a consequence of their evaluation of their suppliers, they had decided on balance not to place any production orders with KTC for the FW2016 season but remained open to meeting with KTC about possible future cooperation.

It appears clear from the historical relationship between the parties that SMS for the Fall/Winter seasons were normally ordered between end of May and early June each year. It was also normally the case that the SMS for Fall/Winter products were shipped by KTC to Haglöfs around end of September to early October each year. Haglöfs state in their submission that in the best of situations SMS should be shipped for a Fall season at the end of September.

It appears that Haglöfs would normally place their initial forecasted production requirements for their Fall/Winter production to KTC during the second half of September, with the actual production orders being placed during the forecast periods in order to give KTC as long a production lead-time as possible. Therefore, in the case of the FW2016 collection, events appear to have been broadly in line with what could be regarded as the usual practice between the parties and in line with normal expectations.

The sequence of events as stated above leads to the following conclusions:

1. It seems from their submissions that Haglöfs had been undergoing a strategic review of the future direction for their brand since November 2014 and that their sourcing plans were part of this review. They have clearly stated that their aim was to reduce their number of suppliers they worked with by 50%. It would appear that KTC were unaware of such a planning review by Haglöfs. They also confirmed that they did not communicate their final decision in respect of this strategic review to KTC ahead of their email on 22nd September 2015. It is somewhat understandable (even in the case of a long relationship together) that Haglöfs would not wish to have made the details of this review explicitly known externally until it was completed. Haglöfs have also stated that the actual decision about re-sourcing their products was not finalized until September 2015. However, with some prior understanding of strategic review processes, it seems remarkable that Haglöfs did not know between November 2014 and September 22nd 2015 (some 10 months) of their likely, or possible, decision not to work with KTC for the FW2016 collection, nor to have appreciated what problems this may create for KTC. Maybe significantly, this decision was communicated to KTC 4 days after KTC shipped the SMS for FW2016 to Haglöfs. A suspicion from this timing could be that Haglöfs waited until after they knew they would get supply of their SMS samples before communicating their decision to KTC. At best, this timing is highly unfortunate, but at worst it can be viewed as commercially understandable but also unethical.
2. It appears from Haglöfs’ submissions that they had some grievances with the way the business with KTC had been developing. They make reference to

issues they had with KTC's flexibility, such as lead-time, prototypes, samples and production planning. However, they also state that KTC scored positively in terms of quality and delivery. They also refer to what they saw as a decline in services that KTC provided. However, there was no evidence provided in Haglöfs initial submissions to demonstrate that these views had been communicated to KTC in written form until their email sent on 22nd September. During the complaints report review process, Haglöfs did produce an email chain that reflected a degree of dissatisfaction over the development timeline for the SS2015 range. These emails show that there was some degree of frustration highlighted by Haglöfs in respect of the KTC development lead times. Haglöfs do say that the issues were discussed openly with KTC at the OutDoor Show in July 2015 but KTC did not share the same view of this meeting. In contrast, KTC did not have the impression that the cooperation between themselves and Haglöfs did not work properly, nor that KTC was not following the production-planning schedule. KTC do concede that there had been some times during their relationship with Haglöfs that there had been some late deliveries, but they say that they notified Haglöfs at the earliest stage possible about any such delays. They also submit that during the last two seasons of supply there had been no late deliveries to Haglöfs. KTC acknowledge that there had been negotiations or discussions on which KTC and Haglöfs had differing views. However, they clearly had not expected a sudden break in the working partnership with Haglöfs in the form of no production orders for the FW2016 collection. In support of their view, they state that following the email of 22nd September from Haglöfs, announcing that they would get no orders for FW2016, they received subsequent emails from Haglöfs team members expressing their thanks for their cooperation and *"flexibility, willingness to help with special enquiries, prompt response, problem solving and the nice way of communicating"*. This KTC submit does not indicate a relationship that was not working properly. Additionally, they refer to an email from Haglöfs' Material and Buying Manager in November 2015 thanking KTC for their *"great cooperation over the years"*. They also cite an email they received from Haglöfs on 10th September 2015 thanking them *"very much for your cooperation, flexibility and dedication, it is really appreciated"*. It could be explained that these were simply pleasantries from the staff at Haglöfs towards KTC after many years of working together but they do not speak of a deterioration in relationship that could lead to a sudden withdrawal or orders for the FW2016 collection.

3. KTC had clear information that their business with Haglöfs was in decline from 2014. Interestingly, for the FW2016 season they were only being asked to produce SMS for 4 x Carry-Over styles. They were not being asked to sample any new products that Haglöfs were developing. KTC state that while the decline in business with Haglöfs was of course not welcome, they believed that given the market situation and unfavourable weather conditions, only making 4 carry-over styles was not an illogical approach by Haglöfs. This does, however, speak significantly about the trend of the business relationship and what could reasonably be expected as a further decline in business from Haglöfs. In situations like this, business relationships can eventually decline to the point that they become uneconomical and unsustainable for both sides. With just 4 carry-over styles to develop, it would not be unreasonable for KTC to suspect a possible future ending to the relationship with Haglöfs. KTC admit that they did not foresee such a problem and did not seek clarification from Haglöfs as to their intentions in only running 4x carry-over styles with them. KTC were also

questioned about why they did not respond more quickly and positively to Haglöfs' proposal for an *'open and honest'* discussion about possible future cooperation together in the communication on September 22, 2015. KTC stated that the prior decision made by Haglöfs to cancel their production of another product that KTC had developed for them for the SS14 collection, with a similarly unacceptably short-notice, had in their view been a first break in trust for them. When this second incident occurred for the FW2016 production, they felt that there was *"hardly any open and honest practice in the behaviour and operation"*. It seems evident that, correctly or otherwise, their trust in Haglöfs had been broken and that they felt that there was no future in the relationship with Haglöfs.

Based on the above, it seems clear from the information provided that an irretrievable breakdown in relationship seems to have occurred between Haglöfs and KTC. It is hard not to conclude that either one party was not transmitting its message clearly enough and/or the other party was not receiving it clearly. The conclusion therefore has to be that there was a significant failure in communication and understanding between the parties.

In the industry, there is a common practice that operates in the relationships between most brands and factories. It is understood that making samples is a high cost operation because of the relatively small production numbers involved. Often factories will make a surcharge for producing samples but often they 'absorb' some or all of this cost and recover it in the margin made on the subsequent volume production. Therefore, for factories making commercial production of products, it is critical to recover their costs on sample production. Equally, factories will build relationships with brands and will either firmly or tentatively 'reserve' production capacity for that brand in their master production planning schedules. It is common practice for most brands to follow similar ordering schedules and most brands make commitments to factories at a similar time of the year and well ahead of the actual main production. If, as in this case, production is then 'pulled away' from the factory late in the cycle, it can be difficult for the factory to replace this lost production. This, in turn, can have an impact on a factory's ability to maintain its workforce commitments with the possibility of limited working times or lay-offs. This failure in responsible purchasing practices affects the ability of brand and factory to improve working conditions that lies at the heart of the Fair Wear Foundation membership of both members.

In conclusion, it is hard not to come to the conclusion that having been in a strategic review of their operations and sourcing plans since November 2014, Haglöfs would not have known before 22nd September 2015 that they were unlikely to place any production orders with KTC for the FW2016 season. From a brand perspective, it may even be that Haglöfs was concerned that if they did make early reference to their possible decision, KTC would seek another brand and allocate their production capacity elsewhere, or maybe even hold back the SMS samples as a leverage item in their relations with Haglöfs. However, to have allowed KTC to produce the SMS samples and provided production forecast dates to KTC and yet give no indication that this business might not be placed with KTC does not reflect well on Haglöfs. Equally, it would seem reasonable that Haglöfs would (or should have) understood that this would cause KTC problems that they might have been able to alleviate with more notice.

Some of the timings of events surrounding the SMS are also unfortunate. The SMS were shipped by KTC to Haglöfs on the 18th September 2015. Just 4 days later, on the 22nd September, Haglöfs inform KTC that they will place no production orders for the FW2016 collection. It is difficult not to draw the conclusion that this decision was only transmitted to KTC after Haglöfs knew that their SMS samples had been shipped to them. This seems inconsistent with operating a fair working relationship with a supplier they had worked with for more than 10 years. In terms of purchasing practices, this relates to indicator 1.6 of the current Brand Performance Check methodology, as Haglöfs' production planning systems did not support the factory in having reasonable working hours.

When it comes to KTC, it appears from the information provided that they have been relatively reactive in their relationship with Haglöfs. It appears that they did not seek out more information about the state of the business for the products they were making for Haglöfs, or adequately registered the concerns that were being raised by Haglöfs and their possible implications for future business. At the very least, to see the business between themselves and Haglöfs in decline and to be told that they were only being asked to produce 4 carry-over styles should have alerted them to a possible more serious problem for the future. Just as brands need to understand and play an active part in their relationships with their retailer customers, in order that they may better understand their business, then equally it would be beneficial for factories like KTC in the interests of their own business, to become more involved and proactive in their relationships with the brands they supply. It can only help KTC to understand more about the wider context that the brands are operating in and the possible implications for the future.

It appears evident that a more open relationship and dialogue between Haglöfs and KTC over the last year might well have helped to avoid the problems that gave rise to this complaint. It is then also strongly recommended that future discussions about key matters be supported by clear written documentation after the meeting to ensure that there are no misunderstandings, especially where important matters with significant consequences are discussed. Connected to the issue of the relationship between the parties is also the subject of the quality of the communications. There would appear to be a greater need for an improved communication between brand and factory. It is clear from the submissions from both sides that they both held quite differing views about the state of their relationship.

In subsequent communication, FWF inquired of KTC what kind of impact the withdrawal of the order has had on the workers, as per the rationale for the complaint. While it is difficult to accurately assess the impact of the complaint to a single cause, considering the number of workers and the number of brands that KTC produces for, KTC did indicate that the lost production space has not yet been replaced. Since the loss of Haglöfs' production placement, KTC has seen a 10% reduction of its knit sewing workers (around 1% of the total workforce). In absolute terms, KTC indicated that this was about equal to the number of workers that would have been working on Haglöfs production in two production lines.

9. Remediation

Based on the findings and conclusions as drawn by the independent garment industry expert, FWF concludes that Haglöfs was detrimental to its and FWF's shared goal of improved working conditions at its supplier KTC when it made the decision to pull its orders for FW2016 at a relatively late stage.

At the same time, KTC should have been alerted to potential problems with Haglöfs production when it received only 4 carry-over styles for FW2016 and could potentially have acted in a more proactive manner and inquired about Haglöfs' and its partnership.

In terms of remediation, FWF believes this to be an important complaint, as it relates Haglöfs' purchasing practices to the impact that it had on the factory. FWF requires Haglöfs to demonstrably and substantively improve its purchasing practices regarding supplier selection, production placement and exit procedure purchasing practices. Specifically, it expects Haglöfs to demonstrate to FWF that it has taken steps to prevent similar situations from happening in the future. These steps must be specified in Haglöfs next Annual Workplan and their implementation reported on in its Annual Report.

10. Verification

This complaint relates to the purchasing practices of Haglöfs, and remediation will take place as described above. Verification of remediation steps will be part of the next Brand Performance Check conducted (most specifically for Indicator 1.6), and will be publicly reported on in that document.

11. Evaluation by the complainant

KTC as complainant reacted positively to the results of the investigation. In terms of remediation, it would also appreciate an official statement and/or apology from Haglöfs management with regards to this complaint.