

# Forced labor

## An escalating risk impacting the bottom line (Part 1)

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The COVID-19 pandemic has amplified a global movement driven by investors and consumers for companies to put purpose over profit. There has been intensifying scrutiny concerning human rights issues that include:

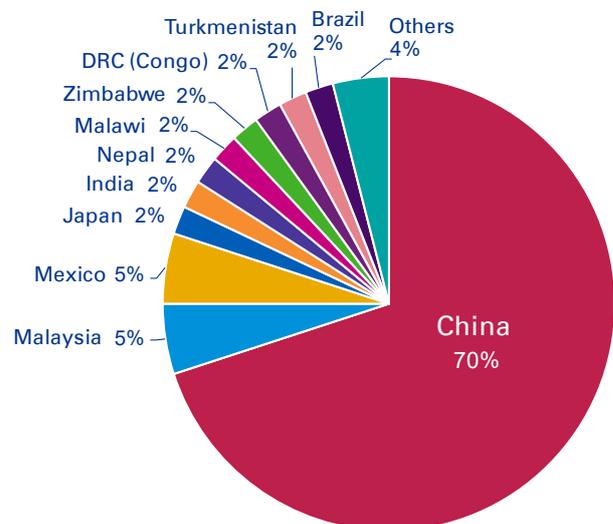
- 1 Forced labor, child labor and other slavery-like practices
- 2 Unsafe or unhealthy working conditions
- 3 Discrimination by race, age, gender, sexuality and other protected attributes
- 4 Displacement of local communities
- 5 Underpayment for labor or services provided

But a typical executive response on the issue remains “What has human rights to do with us?”. The short answer is, plenty.

The U.S. Customs and Border Protection (“CBP”) issued Withhold Release Orders (“WRO”), effectively preventing the imported goods from entering the United States if suspected to be produced by forced labor. CBP has specifically targeted imports from countries susceptible to forced labor, which included four companies from Malaysia.<sup>1</sup>

In fact, based on the updated active list, Malaysia has the second highest number of companies in the WRO – second to China.

**Current active WROs per country**



1. [U.S. Customs and Border Protection \(CBP\) Withhold Release Orders and Findings](#)

Source: U.S. Customs and Border Protection (CBP) Withhold Release Orders and Findings, as at October 2020

The U.S. is Malaysia's third largest trading partner; exports to the U.S. registered a double-digit growth of 12.7% in 2020 to RM108.81 billion, the highest export value in the last decade. The expansion was boosted mainly by manufactured goods which increased by 13.1% to RM106.15 billion and accounted for 97.6% of Malaysia's total exports to the country.<sup>2</sup> Hence, any sanctions from export market authorities will have a severe impact in Malaysian companies' trade growth over the long term.

Prohibitions against importing goods produced with forced labor have long been a part of the law in the U.S., and sanctions on Malaysian companies may cause multiplier effects that would impact our country's standing on the global competition landscape.

There are also indications that jurisdictions in other parts of the world are considering imposing similar enforcements in the near future. On 12 January 2021, UK and Canada became the latest countries to impose new policies on imports as measures to combat forced labor and human rights violations.<sup>3</sup>

Increasingly, there have also been reported cases of legal actions against businesses over human rights issues; the Business and Human Rights Resource Centre lists more than 200 active cases on its website.<sup>4</sup>

In recognition of these activities, the Malaysia Emergency Ordinance (Workers' Minimum Standards of Housing and Amenities) 2021 was enacted on 17 February 2021 and the Act 446 is now enforceable in Sabah and Sarawak as well. The Ordinance gives authority to the Director-General of the Labor Department to order owners of accommodations to replace, change or upgrade the facilities should it be found not to meet criteria under the Act 446.

Stiffer penalties against employers or owners of accommodation for failing to provide proper housing facilities for workers and who fail to comply with the order can be fined up to RM200,000 or be jailed up to three years, or both.<sup>5</sup>

However, it should be noted that the legislation does not address the greater human rights issues in Malaysia vis a vis the twin threats of human trafficking and forced labor.

## Risking the bottom line – spotlight on Malaysia

Failure to identify and respond to human rights issues will not only lead to costly and disruptive legal actions but can also cause investor divestment, negative publicity, reputation damage and significant financial loss.

Sceptics need only refer to several widely reported human rights cases that emerged out of Malaysia recently, which were brought to light because of the COVID-19 contagion among migrant workers.

In the case of the world's largest glove manufacturer, which drew national and international attention, over 1,000 of the company's contract workers were infected giving rise to community spread. Investigations revealed the source of the contagion was found in the housing facilities provided to its workers.

Subsequent enforcement operations in five States — Perak, Kedah, Kelantan, Negeri Sembilan and Johor — resulted in the Ministry of Human Resources (MoHR) opening 19 investigation papers against six companies related to the company under the Workers' Minimum Standards of Housing and Amenities Act 1990 (Act 446).<sup>6</sup>

The impact to the company was immediate; shares declined 17% with about RM11 billion in market capitalization reportedly wiped out. The glove maker had also spent over RM1 billion — more than half its FY2020 earnings — repurchasing its shares.

Unfortunately, this is not an isolated case. Since Malaysia's Act 446 came into force on 1 Sept 2020, MoHR had carried out about 100 operations nationwide to check on workers' living conditions. A total of 23 companies have been charged in court for failing to comply with the government's ruling on the provision of workers' accommodation.<sup>7</sup>

It is clear from these examples that managing human rights is not only about doing the right thing — it is also about protecting the bottom line. Business leaders must acknowledge that every business, partnership or sourcing decision entails significant questions about potential human rights issues. This reality demands a shift in thinking — away from traditional risk-to-business concerns and towards non-financial risk-to-people concerns.

2. [Malaysia External Trade Statistics 2020](#), Weekly Bulletin, Volume 623. Ministry of International Trade and Industry. 2 February 2021

3. ["UK and Canada Announce New Measures to Combat Forced Labor and Human Rights Violations"](#). Retail & Consumer Products Law Observer, 27 January 2021

4. [Business and Human Rights Resource Centre – Lawsuits Database](#); Data retrieved on 29 January 2021

5. [MOHR Press Statement](#) released on 19 February 2021

6. ["Govt opens 19 investigation papers on Top Glove worker lodgings in five states"](#), Malay Mail, 1 December 2020

7. ["Not complying with workers' accommodation requirements, 23 employers charged"](#). BERNAMA, 29 January 2021

## Where to begin on the human rights journey?

To be clear, human rights risk goes beyond working conditions for workers to also encompass aspects across the enterprise, including:

- 1 Suppliers and partners in the value chain
- 2 Acquired businesses or activities in new global markets and regions
- 3 Project financing, loans, asset-management services, and more.

To begin with, Boards need to ask 3 crucial questions of their management team:

### 1 Do we fully understand how human rights issues can impact our company – today and in the future?

**What will be the impact to our brand or business sustainability if we fail to manage our human rights risk?** The UN Principles for Responsible Investment (UNPRI) has noted that

2 institutional investors bear responsibility to respect human rights, under the UN Guiding Principles on Business and Human Rights (UNGPS) as adopted by the UN Human Rights Council and the OECD in 2011. The UNGPS has driven expectations that the institutional investment community will start addressing the issue of human rights in their investment review process. Given that both EPF and KWAP are signatories of the UNPRI, this increases risks for Malaysian businesses.

3 **Who in our company is accountable for human rights issues?** Corporate accountability cannot be discounted in relation to human rights management despite the lack of legislation. The recent Securities Commission's Guidelines on Conduct of Directors of Listed Corporations and Their Subsidiaries clearly states the Board has oversight of group financial and non-financial performance, business strategy and priorities, risk management including material sustainability risks and corporate governance policies and practices.

Awareness of human rights across the organization and prioritizing them is only the beginning in the process to address these risks. In our second part commentary, we will cover KPMG's seven-step strategic approach to analyzing human rights risks and key considerations companies should incorporate in their human rights journey.

Ultimately, managing human rights risks effectively can enhance a company's social license-to-operate, build trust and achieve better outcomes for both the company and society.

#### Read also:

[Prevention is better than cure \(Part 2\)](#)

To explore the implications of human rights risk in your company, reach out to KPMG's professionals:



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