

Promoting decent work in export processing zones (EPZs) in Sri Lanka

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Introduction

Over the past three decades export processing zones (EPZs) have become popular instruments of trade policy, offering enterprises located in them free trade conditions and a liberal regulatory environment. Many countries see export promotion as an important policy for economic growth in developing countries. Various measures are being adopted by the governments in these countries to promote export competitiveness. As a policy means of achieving this goal, the concept of EPZs has gained noticeable significance in recent years. Terms such as EPZs, free trade zones (FTZs), special economic zones (SEZs) and export processing factories (EPFs) refer to similar concepts, with variations in policy prescriptions and objectives. As EPZ is most commonly used, this paper uses it interchangeably with FTZ and SEZ.

In creating the EPZs, the immediate goal for Sri Lanka was to generate direct foreign investment, exports, foreign exchange, and employment. As in most countries, in Sri Lanka EPZs do not account for a large percentage of the total national employment but gains must be weighed against the cost of generating the benefits of EPZs, in particular the possible loss of taxes and revenues.

The basic objective of this paper is to examine emerging issues concerning EPZs in Sri Lanka, focusing on decent work, and setting out recommendations to address these issues.

EPZs provide customs-free and tax-exempt, export-oriented manufacturing facilities, investment incentives and streamlined administration, cheap utilities, and better infrastructure. According to Jayanthakumaran (2002), most enterprises in EPZs are engaged in processing intermediate imports for exports. Also included are labour-intensive light manufacturing such as garment production, assembly of light electrical goods and electronics. Among the benefits offered are exemption from: some or all export taxes; some or all duties on imports of raw materials or intermediate goods; direct taxes such as profits taxes, municipal and property taxes; indirect taxes such as VAT on domestic purchases; national foreign exchange controls. Foreign companies also benefit from free profit repatriation. EPZs offer streamlined administrative services, especially to facilitate import and export, and provide free enhanced physical infrastructure for production, transport and logistics (Milberg, 2007).

EPZs are the mechanism through which global production chains are elaborated, and their prospects are closely linked to the dynamics of global investment and trade. EPZs evolved mainly because as production costs rose in developed market economies, companies shifted the labour-intensive parts of the production process offshore, where EPZs provided an attractive base.

Enterprises either set up their own plants, or build up a network of subcontractors with whom they work very closely in order to ensure that

performance is satisfactory. Given the current trend towards verticalization, major brands concentrate only on the design and marketing of their brand, while subcontracting all the manufacturing activities. The subcontractor sources the materials and components, manufactures the article and performs the necessary quality controls. If any of the time, cost or quality limits are not met, the subcontractor bears the cost and may lose future contracts to competitors.

In Sri Lanka, EPZ activities include goods production and assembly to services, including information processing, telecommunications, business process outsourcing (BPO), hotels, power generation, etc. As in most countries in Asia, Africa and Latin America, the largest share of investment was absorbed by the textiles and garments sector. Today there are about 300 enterprises within the bonded zones and 1,200 establishments receiving similar benefits outside the zones.

The main findings in this paper can be summarized as follows:

- The presence of EPZs has grown over the past 30 years, in terms of the number of zones, employment, and share of exports.
- This growth has been most marked in two zones, namely Katunayaka and Biagama, both outside Colombo, the capital city.
- Despite this growth in EPZ activity, EPZs still make up a relatively small percentage of population. “EPZ intensity” (calculated as EPZ employment as a share of national employment) for 2006 was 1.67, compared to Mauritius which was 17.74 per cent.
- Wages in EPZs continue to be at or slightly above wage levels outside EPZ areas, while the female composition of EPZ employment is possibly declining due to a tightening of the labour market for female workers.
- There appears to be an improvement in the degree of enforcement of labour standards and rights in EPZs compared to the situation in 1997 as a result of social audits and the reorganization of the labour inspectorate.
- The completion, in 2004, of the phase-out of apparel quotas under the Agreement on Textiles and Clothing, did not significantly affect Sri Lanka and has remained cost competitive.
- EPZ firms still do not form links to the domestic economy, in most cases purchasing almost all their inputs from abroad. demand expansion would ease this structural obstacle to growth.
- The distinction between EPZs in the bonded area and outside is diminishing as the same conditions are being extended to 1,200 establishments outside the enclaves. As the EPZ/non-EPZ distinction diminishes, the issue of labour standards and their enforcement will become a key issue.

The outline of this report is as follows: section 1 describes the macroeconomic perspective and the labour market scenario; section 2 deals with the labour administration system; section 3 describes the evolution of the EPZ policy in Sri Lanka; section 4 deals with the analytical framework on key labour issues. Section 5 concludes the analysis and draws policy implications.

1. Sri Lanka's macroeconomic perspective

Since the late seventies, Sri Lanka has looked to a liberalised economy and economic growth as key to development. However, despite a reasonable record of economic growth, poverty has not been reduced. According to the 2006 Central Bank Report (CBR 2006), Sri Lanka recorded a 7.4 per cent growth rate – the highest since 1978, and an unemployment rate of 6.5 per cent. However, unemployment and underemployment among the youth is still a serious problem which the government is trying to address. Despite the favourable developments, emerging inflationary threats and the overall security situation posed serious challenges for policy-makers. One of the key policy thrusts was persistently directed towards curbing the rising inflation pressure. The average annual inflation stood at 13.7 per cent in 2006. Inflationary pressures pushed up annual consumer price inflation to an average of 18.9 per cent in January-April 2007, with serious consequences for the labour market, including workers employed in the EPZs.

The economic outlook in Sri Lanka for 2007-08 will largely depend on the internal security situation (EIU, 2007) *Details for biblio pls*. In 2006, exports performed relatively well, supported by steady garment export growth as investment projects in the sector were implemented. The garment sector has in the past benefited from Sri Lanka's inclusion in the European Union's Generalised System of Preferences scheme, which grants tariff reductions to participating countries.

The labour market scenario

Labour force and employment

According to the latest labour force surveys conducted by Sri Lankan Department of Census and Statistics (DCS, 2006), the midyear population of Sri Lanka was estimated at 19.9 million in 2006. Of this, the labour force was 7.6 million, comprising 7.1 million employed and 0.5 million unemployed. Another interesting labour market development in Sri Lanka is the large size of the public sector. One in every ten workers in employment is employed in the public sector. Furthermore, as 35 per cent of the workforce are employed in the formal sector, the size of the informal economy is relatively smaller compared to countries such as India, Pakistan and Bangladesh.

Wages

Wages in the public sector are largely determined by the government. For formal private sector employees, the wage-setting mechanism includes several forms: tripartite determination, collective bargaining, remunerative tribunals, individual employer-employee contracts, and more recently, decisions and adjustments by government directives. In the informal private sector, wages are mostly determined based on demand and supply conditions in the market (CBR, 2006).

The minimum wage fixing system prevailing in the private sector comprises 43 sectoral Wage Boards which include workers in the EPZs. However, one of the current weaknesses of the Wage Board is that it does not cover *certain* categories of employees in the EPZs.

A recent ILO study (2007) noted that wages, especially in the private sector, were very low wages and showed a decline in real wages over the years. There has

been an increase in the gap between wages in the private and the public sector where wages are double than those in the private sector.

The study also pointed out the growth in the wage gap by sex and region, as well as the issues of wage-fixing and workers' rights in export processing zones. Wage bargaining is limited at both the sectoral and enterprise level and collective agreements have over the years reduced in number and coverage. The study brought home the fact that there was no link between wages and productivity and/or economic performance. While trade unions insist on the need for setting wages that ensure decent living standards, especially in the private sector, employers stress the need to develop policies to curb inflation and pay systems that link wages to enterprise performance, in order to keep their competitive position. The table below shows that real wages for workers in industry and commerce have fallen in 2006 in the private sector. For industry and commerce as a whole, real wages fell by 11 per cent.

Table 1. Wage rate indices

Employment Category	Index						Percentage Change					
	Nominal			Real			Nominal			Real		
	2004	2005	2006(a)	2004	2005	2006(a)	2004	2005	2006(a)	2004	2005	2006(a)
1. Government employees												
Central government employees	1.872.1	2,417.5	3,155.6	123.3	142.7	164.2	22.8	29.1	30.5	14.0	15.8	15.1
Non-executives	1.709.0	2,178.4	2,853.8	112.5	128.6	148.5	21.2	27.5	31.0	12.6	14.3	15.5
Minor employees	2.039.5	2,672.4	3,474.1	134.3	157.8	180.8	24.6	31.0	30.0	15.7	17.5	14.6
Government school teachers	1.428.4	1,818.6	2,304.2	94.1	107.4	119.9	21.0	27.3	26.7	12.4	14.1	11.7
2. Workers in wages boards trades												
All wages boards trades	1.233.0	1,329.7	1,358.2	81.3	78.5	70.7	2.3	7.8	2.1	-4.8	-3.5	-9.9
Workers in agriculture	1.397.7	1,527.4	1,567.1	92.2	90.2	81.6	1.1	9.3	2.6	-5.9	-2.3	-9.5
Workers in industry and commerce	1.044.1	1,078.4	1,090.7	68.9	63.7	56.8	3.4	3.3	1.1	-3.7	-7.6	-10.8
Workers in services	751.0	779.7	779.7	49.5	46.0	40.6	10.8	3.8	0.0	2.9	-7.0	-11.8

(a) Provisional

Source: Department of Labour

Source: Central Bank Report, Sri Lanka. 2006.

However, labour productivity continued to improve in 2006, following the trend of the last few years. In terms of value addition, it increased by around 3 per cent compared to the previous year, to Rs.142,700 per employee, based on the employment numbers adjusted for the Northern and Eastern provinces for 2006 (CBR). The considerable increase in productivity in the services sector was the main contributor to the increase in productivity in 2006 while the contribution from the industry sector was marginal.

The labour relations framework

The constitution of Sri Lanka recognizes the fundamental right to organize trade unions and the freedom to join unions. Sri Lanka has also ratified all the fundamental ILO Conventions. Under the Trade Union Act (TUO No. 14, 1935), the right to form and join a trade union is a core right of every citizen. The rights, immunities, and governance of a trade union are provided for by the TUO. The status of trade unions was enhanced further by an amendment to the Industrial Disputes Act which became operative in December 1999, which according to trade unions facilitated trade union organization in the zones. This amendment compelled mandatory recognition of a union that had a membership of 40 per cent of the workforce by defining refusal to bargain with such a union by the employer as an unfair labour practice. Other acts of the employer, such as interference in the

activities of a trade union, were also declared as unfair labour practices (Sharmila and Shamali, 2001). The Employers' Federation of Ceylon, the apex organization of employers, continues to see the amendment as one-sided and not clearly defining the activities of workers which could constitute unfair labour practice,

Prevention and settlement of disputes

For the purpose of settling disputes, the employer and employee have the right to settle a dispute internally, by mutual agreement or by entering into a collective agreement. The Industrial Disputes Act provides for the intervention of the Commissioner of Labour through a number of mechanisms. A dispute may be settled by conciliation or mediation between the parties, or it may be referred to settlement by an industrial court or arbitrator (Sivananthiran, 1999).

The Commissioner also has the power to summon parties and conduct any inquiries he considers necessary where he believes an industrial dispute exists. Employees and trade unions may also resort to trade union action, including strikes, downing of tools, picketing, etc., to obtain their demands and rights from employers.

According to the latest available data for the period January to June 2006, the Department of Labour dealt with a total of 4,269 disputes (DOL Administrative Report, 2005). During the same period, the conciliation machinery of the Ministry of Labour settled 3,948 of these disputes – a commendable effort. The Ministry employs about 400 labour inspectors; labour inspections for the year 2005 dropped overall (DOL Labour Statistics, 2005).

Collective bargaining

In 2005 and 2006 an average of 40 collective agreements were concluded by workers and employers (DOL Labour Statistics, 2005). The number of strikes in 2006 were the lowest recorded in the last 10 years. However, some disputes and continuing worker unrest in some key public sector institutions (such as the Sri Lanka Railway, Ceylon Electricity Board, the Sri Lanka Ports Authority and Ceylon Petroleum Corporation) during the same year (CBR) have raised concerns as to maintaining overall industrial harmony. Over the years, public sector disputes have been increasing and the Government has requested ILO assistance in strengthening its dispute settlement machinery. In the private sector, particularly in the EPZs, rising inflation has led to negotiations in some enterprises between the unions and employers for higher wages.

Terms of employment

While employers and employees are generally free to contract the terms of employment by mutual agreement, several statutes establish minimum standards. The Shop and Office Employees' (Special Provisions) Act specifies minimum leave entitlements, payment of wages, maintenance of records and registers; the Factories Ordinance provides for minimum standards of health safety and welfare for workers employed in factories. According to the terms of the Wages Board Ordinance, a number of Wages Boards were established for specific types of activities, and these Boards determine wages by a tripartite discussion (Sharmila and Shamali, 2001).

Labour inspection

According to the Industrial Disputes Act, the Commissioner of Labour, any labour officer or any other prescribed officer has “the power to enter and inspect at all reasonable hours of the day or night any place in which any workmen are employed, for the purpose of examining any register or record” (required to be maintained under the Act). The inspecting officer also has the right to require the production of registers and records at a place of his choice, to make copies of all such records, and to interrogate any person whom he finds at the workplace and whom he has reasonable cause to believe is an employer or a workman. Any expenses incurred in this regard are met by the state. The 2005 Annual Report of the Ministry of Labour indicates that the number of inspections under the Wages Board Ordinance, the Provident Fund, and the Shops and Office Act all declined in 2005 compared to 2004.

2. The evolution of free trade zones in Sri Lanka

Sri Lanka attained political independence in 1948. However, the process of industrialization began only in the late 1950s when the government formulated a new development strategy with emphasis on industrialization (Abeyratne, 1997). The industrialization policies initiated during this period were influenced by contemporary development thinking, hence based on the Import Substitution Industrialization (ISI) strategy. For about two decades until 1977, Sri Lanka remained a paradigm case of an inward-oriented trade regime (Aggarwal, 2003; Abeyratne). By the late 1960s, however, the balance of payment situation had worsened in Sri Lanka and a new policy emphasis on export promotion was placed within the overall framework of the ISI strategy.

In 1978, the government set up the Greater Colombo Economic Commission (GCEC) with wide ranging powers to facilitate foreign direct investment (FDI) in the fully export-oriented ventures. The immediate goal for the country was to generate foreign direct investment, exports, foreign exchange, and employment – all of which would not be created without the EPZs.

Following the establishment of the Katunayaka zone, the BOI became involved in massive expansion in EPZ schemes. Today there are 12 new EPZs; table 3 shows the employment generated in each of these zones by gender.

Table 2. EPZs: Employment statistics 2007 (within bonded area only)

Zone	Male	Female	Total
Katunayake	16406	34069	50475
Biyagama	9338	10649	19987
Koggala	1810	8254	10064
Mirijjawila	168	1207	1375
Seethawaka	5839	9515	15354
Horana	560	138	698
Kandy	324	216	540

Zone	Male	Female	Total
Wathupitiwala	1308	4443	5751
Mirigama	669	1454	2123
Malwatta	616	2001	2617
Mawathagama	911	2228	3139
Polgahawela	590	1304	1894
Total	38539	75478	114017

Source: BOI, document handed during interview

Thus, the EPZ policy in Sri Lanka was designed primarily to attract foreign investment and foreign exchange within the framework of the export-oriented policy regime: with significant relaxation of rules governing FDI, developed infrastructure and support services, freedom from diverse industrial regulations, high quality governance, and other attractive incentives. All the zones are generally located in industrially developed districts. Special efforts are made to promote zones outside Colombo, and certain complimentary incentives are offered to the investors there. These include additional tax holidays, concessionary turnover tax, and lower ground rent. It is estimated that the garment sector in 2005 itself provided direct employment to approximately 340,000 people, 87 per cent of which were women. Another 600,000 workers were indirectly dependent on the industry through employment in a range of support and related service occupations (ILO, 2005).

The Katunayake EPZ (KEPZ) is the most highly developed of all the BOI zones, currently with 90 enterprises operating in the facility. Of these enterprises 24 are apparel exporter plants. However other sectors are also represented, such as precious stones and jewellery (5), trading houses (5), hosiery and yarn (4), glove production (4), electric and electronics (4), footwear (3), artificial flowers (3), bags and tents (1), and rubber products (1) .

The Katunayake EPZ companies belong in the most modern sector of the Sri Lankan economy. Exports earnings from the zone totalled 97,186 million rupees in 2006 (BOI, 2007). There are investment projects from 17 countries – 12 enterprises from Hong Kong, 12 American, 10 British, 10 Indian, 10 German, 7 Japanese, 6 Sri Lankan, 4 Belgian, 4 Italian – in addition to companies from Taiwan, Korea, Singapore, China, Luxembourg, France, Sweden and Norway.

In nearly three decades, the zone has contributed to the creation of new job opportunities. When the KEPZ was started in 1978 there were only 261 employees working for the two enterprises established in the zone. In 2007 the zone has a workforce of 34,920 local employees and 197 expatriates and has thus brought employment opportunities to a large number of women workers. The table shows employment in the KEPZ has declined somewhat from 1995 due to the relocation of factories to other countries and to other regions in Sri Lanka, technical upgrading, changing employment relationships and shortage of workers. Currently there is a shortage of 15,000 workers in the various EPZs in the country.

The Board of Investments (BOI)

In Sri Lanka the BOI is the apex EPZ authority. As in many other countries the BOI operates a one-stop centre for foreign investments. It has its origins in the Greater Colombo Economic Commission and is directly responsible to the President of Sri Lanka. Operating as an autonomous body, it functions as a central facilitation point for investors, providing advice and assistance at every stage of the investment process, and is thus the only organization that an investor needs to contact. It is important to note that the BOI is responsible not only for the promotion of EPZs but also for all other foreign direct investments .

The BOI is empowered to grant special concessions satisfying special eligibility criteria. The mechanism through which such concessions are granted is the agreement which modifies, exempts, and waves BOI regulations pertaining to inland revenue, customs, exchange control and import control. From time to time, the incentives have been expanded to drive Sri Lanka's two-pronged strategy of diversification of exports towards advanced technology and value added and investments in large-scale projects (including infrastructure) (Aggarwal, 2005).

To attract FDI in the initial phase of the evolution of the zones, the government granted generous tax concessions which allowed foreign ownership, a tax holiday of up to ten years including no taxes on the remuneration of foreign personnel employed and on royalties and dividends of shareholders, as well as duty exemptions on the importation of equipment, construction materials and production inputs. In early 1979 the BOI introduced the Foreign Currency Banking Units Scheme, which provided the EPZ units unlimited access to foreign currency credit at interest rates prevailing in the world financial markets.

The BOI also provided EPZ units with industrial services such as land, power, water and telecommunication services at subsidized rates. Investors can also own 100 per cent equity in the sectors such as exports, tourism, infrastructure services, dairy and livestock, electronics. Investors other than those above can set up joint ventures, e.g. banking, insurance, energy, and power supply.

One of the unique services provided by BOI is the role of facilitator in the provision of various services to investors. At the time of entry of an investor, the BOI designates an officer to assist and guide the investor in all his dealings with various government departments and with the departments within the BOI (Aggarwal, 2005).

Sectorwise data for all the zones was not available at the time of writing. However, the Director of Labour Relations provided the sector composition for the two most important zones in Sri Lanka, the Katunayaka and Biagama (table 4).

Table 3. Sectorwise distribution of enterprises for the year 2006 in Biagama and Katunayake

Sector	2006
Food and beverage and tobacco	6%
Textiles, garments, leather	50%
Chemicals, petroleum, coal, rubber and plastic	12%
Non metallic mineral products	4%
Manufactured products	8%
Services including agricultural products	12
Others	8

Source: BOI internal document (2007).

As seen in many other countries, in both Katunayake and Biyagama, the share of textiles and garments make up 50 per cent of total investments in 2006. Thus the process of diversification is critical for Sri Lanka. Nonetheless, industrial upgrading has occurred within this sector, with firms moving from assembly to full-package production, in which higher value added aspects of production are included in the process. Within the EPZ-based apparel sector, Sri Lanka is clearly moving towards the upper end of the market and to full-package production. Exports from EPZs continue to contribute a major share to national exports in Sri Lanka, rising from 33 per cent in 2002 to 38 per cent in 2006.

At present, Sri Lanka not only faces stiff competition from other developing countries of South and South-East Asia, but also from China, which has emerged as a dominant force in the global apparel industry. In the higher-value clothing segment, producers such as Malaysia, the Republic of Korea, Singapore and Hong Kong (China) are also now serious competitors. One of the most significant factors affecting the competitiveness of the Sri Lankan garment industry is low productivity. While it has become evident that Sri Lanka cannot compete on low labour costs alone, the emphasis has been shifted to improving the productivity of both labour and the manufacturing operation as a whole.

Within the BOI, the Industrial relations Department handles complaints made by individual workers or workers' councils and resolves industrial disputes. It also provides other services related to human resources such as providing enterprises with manpower resources, setting the terms and conditions of employment, wages and labour standards and providing updated information on employment statistics. There are 30 officials in the Industrial Relations Department spread over the 12 zones.

Recent investment trends in EPZs

According to the BOI, of the total new foreign direct investment in 2006, more than 60 per cent was invested in the telecommunications sector, textiles, apparel and leather industry, hotels, power generation, information technology and business process outsourcing (BPO). Within the industrial sector, the largest share of investment was absorbed by textiles, apparel and leather products, food, beverages and tobacco products, chemical, rubber and plastic products and non-metallic mineral products. Of the 354 approved projects, 82 projects were fully foreign-owned and 87 were joint ventures between Sri Lankans and foreign investors, while

the rest were fully owned by Sri Lankans. Therefore the trend is towards more joint ventures and local investments (CBR, 2006).

The government is of the view that the thrust of the long-term industrial policy is to develop a globally competitive, dynamic and technologically sophisticated industrial sector. The BOI is of the view that industrial policy should encourage innovation and productivity improvement in processes and services. In this regards, the foreign investment is expected to make a vital contribution by providing capital, access to technology and access to markets. To facilitate this process, the government has initiated several measures aimed at strengthening the legal and regulatory framework, providing necessary infrastructure, improving corporate governance, enhancing quality and maintaining standards, and improving the competitiveness of industries.

GSP Plus status

Sri Lanka is the only country in Asia to benefit from Generalised System of Preference (GSP Plus) status: a reduction of import duty to zero per cent on 7,200 items exported to the EU. This is subject to Sri Lanka ratifying all eight core ILO Conventions, all eight human rights covenants, and 11 conventions on the environment. An additional requirement pertains to value addition pertaining to exported items.

The global market access of Sri Lankan exports was expanded further in 2006 with continuous negotiations at multilateral, regional and bilateral fora. The country, while adhering to the commitments given to the World Trade Organization (WTO), engaged in bilateral trade negotiations with India, Pakistan and other regional countries. Trade negotiations with India in 2006 was mainly focused on resolving the problems relating to quantitative restrictions imposed by India for certain exports and further negotiation of a Comprehensive Economic Partnership Agreement (CEPA).

The government is also pursuing negotiations with the EU aimed at rationalizing the stringent rules of origin (ROO) criteria imposed under the GSP Plus scheme, which require Sri Lanka to add at least 50 per cent value addition in the case of apparel exports in order to qualify for such benefits.

Wages and the feminization of employment in EPZs

More than 70 per cent of workers in the zones are women . The large female share in EPZ employment has been well documented, with women accounting for over 70 per cent and sometimes over 80 per cent. Over the last two decades, studies indicate a strong preference for women workers because they are cheaper to employ, less likely to unionize, and have greater patience for the tedious, monotonous work in assembly operations. This is the same situation in EPZs around the globe.

As stated earlier, Sri Lankan labour laws governing EPZs are the same as in the rest of the country. Although labour laws are uniform nationally, there are emerging issues regarding the enforcement of these laws in EPZs and the restrictions on trade union creation and actions, in reference to the longer working hours and the faster pace of work; trade unions face difficulties or are discouraged.

There is lack of data to compare the wages of workers inside the zones with comparable companies outside. The general impression has been that they are at about the same level as wages for equivalent work in the rest of the economy

(table 3). This may be due to factors such as wage regulation by the Wages Board, the need to adjust to inflation as well adjustments made to public sector wages in 2006. Over the last two years, there have been pockets of labour shortages reported in the labour market and the feminization of EPZ employment appears to have peaked.

In the past, EPZs in Sri Lanka, as elsewhere, tended to higher female employment where the skill intensity of production is low; however, in Malaysia, when the EPZ production shifted to higher-technology production, many of the women were able to obtain employment as technicians in the electronics sector (Sivananthiran, 1993).

Table 4. Enforcement of labour regulations – inspections, 1997-2005

Item	1997	1998	1999	2000	2001	2002	2003	2004	2005
(1) Labour inspections conducted									
(a) Under Wages Boards Ordinance (no.)	8,113	8,583	11,137	9,424	10,812	10,890	16,305	16,306	11,334
(b) Under Shop & Office Employees Act (no.)	11,664	13,254	13,397	12,313	12,266	17,385	21,643	26,354	18,396
(c) Employees Provident Fund Act	12,039	16,144	16,667	30,458	43,053	52,495	52,466	61,190	34,105
(2) Arrears of underpayment revealed at inspections									
(a) Under Wages Boards Ordinance (Rs.'000)	4,547.0	8,055.9	7,821.0	7,909.6	15,235.1	102,904.4	61,052.7	61,244.1	28,097.1
(b) Under Shop & Office Employees Act (Rs.'000)	2,375.8	1,508.2	285.2	3,136.3	893.9	1,914.3	432.6	238.7	2,113.8
(c) E.P.F. Act (Rs.Mn.)	243.2	248.1	363.8	475.2	634.9	921.0	602.4	830.8	1,551.9

Source: BOI 2007

EPZs and linkage with the domestic industry

Despite the growth in apparel exports during the last two decades, the development of backward linkages has been poor. The industry is heavily dependent on imported inputs, with the result that the level of value added is low. In addition, the need to import raw materials results in longer lead times, posing another serious threat to the international competitiveness of the industry. It has not been developed due to the high cost of investment required for the setting up of such operations, and the relatively small market. Sri Lanka therefore faces stiff competition from the countries that are well supported by backward linkage industries (e.g., India and China). Backward linkages did not occur mainly because local producers were unable to meet world market standards for price, quality and delivery terms, and more importantly, there was lack of interest from local manufacturers in serving EPZs because of low perceived returns.

The government has taken several measures to promote regional industrialization. Under “Nipayum Sri Lanka” (the 300 Enterprises Programme), incentives were given for industries to relocate in the regions, which included exemption from income tax for 5-10 years and from duties and value added tax

(VAT) for the import of new plant and technologically advanced machinery. This is a major step undertaken to bridge the gap between the incentives granted for BOI and non-BOI projects. Under the 300 Enterprises Programme, many concessions given to BOI investors were extended to local investors as well. Further, factories which were relocated outside the Western Province were allowed to deduct the costs of relocation from their taxable income (CBR, 2006). This will in the medium term blur the EPZ/non-EPZ distinction. The issue of labour standards and their enforcement in local enterprises will pose further challenges to labour administration.

The Budget 2007 provided measures to further develop the domestic industry. Special attention has been placed on the establishment of textile processing zones to develop backward linkages in the apparel industry. Further, the Budget 2007 also proposed the establishment of a technology institute under the supervision of the National Research Council. This is expected to improve the competitiveness of several industries such as textiles, rubber, electronics and minerals.

The EPZ sector is facing several impediments in achieving higher growth. According to the Joint Apparel Association Forum (JAAF), rising energy costs is a burden. Sri Lanka is a net importer of oil and the supply of reliable and affordable energy to the industrial sector is extremely important in order to achieve higher industrial growth. In addition, the Association emphasized the need to resolve the issue of inadequate infrastructure, the rising costs of labour and raw materials, the lack of skilled labour, the lack of technically qualified personnel in the construction industry, rigid regulations in the labour market and the inefficiencies in public sector enterprises.

Findings and major labour issues

Strategies for coping in a post-MFA environment

The Sri Lankan garment industry has experienced phenomenal growth since the late seventies and continues to be the strongest performer as far as the manufacturing subsector is concerned. Furthermore the garment industry had a comparative advantage as a recipient of GSP Plus status and as a result of a bilateral agreement with the United States. In order to address the issues pertaining to adjusting to the post-MFA¹ era after January 2005 with a view to promoting decent work in the EPZs, a workable system of social dialogue between the three partners – employers' and workers' organizations and the government's labour administration system – in working together towards

Sri Lanka has ratified about 40 ILO Conventions, including the eight core Conventions, and its national legal framework contains stringent measures in respect of these and other rights and freedoms at work (DWCP, 2006). For instance, the Constitution of Sri Lanka guarantees the fundamental right to the freedom of association (Article 14(1)).

However, despite this strong legal environment, there are problems in giving practical effect to some rights at work. There are deficits in ensuring the freedom of association, particularly in some EPZs. Collective bargaining is not widely used as a mechanism for dispute resolution.

¹ International trade in apparel and textiles is regulated by a system of bilateral tariffs and quotas known as the Multifiber Arrangements or MFA; quota restrictions were lifted in 2005.

Improving quality and productivity in the garment sector in EPZs

Most garment manufacturers were geared to producing standard garments for the major markets under export quotas. Before the MFA quota ended, 60 per cent of total garment exports were based on quota exports in 2004, and Sri Lanka's dependence on quotas had been steadily increasing since 1995. So far, the sector has done well not only in surviving but in maintaining its share in the total exports; however, it faces intense competition from China and India.

Despite the fact that the Sri Lankan garment industry has achieved phenomenal growth over the last two decades, it faces several challenges as follows:

- Low productivity compared to India and China despite higher literacy levels.
- Inadequate training of managers and workers is an important factor constraining productivity and competitiveness.
- One of the most significant factors affecting the competitiveness of garment manufacturing enterprises is the poor relationship between employers and employees.
- Sri Lankan manufacturers are more likely to invest in technology in order to reduce their labour force.
- Some of the factories currently operating do not comply fully with labour standards, losing potential market share as a result of turnover.
- Poor infrastructure (roads, transport and telecommunications), as well as delays caused by documentation and customs procedures at ports and airports have seriously affected lead time and costs in the garment industry.

Establishing a Compliance Unit within the MOL to secure compliance with the law

Commencing in 2002, the ILO supported a change process within the Ministry of Labour to enable it to adapt to the country's transition to an economy based increasingly on market forces as the means of resource allocation. It recognized the need for the national labour administration system to adjust and restructure to accommodate new policy initiatives. The ILO support enabled the Ministry to re-examine its role in national development, embrace a range of development initiatives, and adopt new approaches vis-à-vis labour protection and industrial relations. The resulting changes and activities have benefited the clients of the labour administration system; however, further action would be necessary to effect these benefits on a larger scale

Some of the outputs included the preparation of a Performance Improvement and Reporting System to guide the Department of Labour in improving staff productivity and overall performance, particularly at district level. A report on "Strengthening the procedural and operational aspects of the labour inspection system" was drawn up, and a new inspection report form was introduced based on an integrated inspection system. The preparation of a master register of all establishments liable to inspection has also commenced. Advice has been provided

on the nature and purpose of the newly set up National Institute of Occupational Safety and Health and the Institute for Labour Studies.

The restructuring also led to the establishment of a Compliance Unit to secure compliance with labour laws in BOI factories. Its work began with a study of decent work in the garment sector, but since the resignation of the unit chief (to become the Director of Industrial Relations in the BOI itself), it has lost direction. The task in the area of securing compliance and in coordinating with private systems of assessment is a big challenge.

Tripartite action plan

Another initiative supported by the ILO was the development of a tripartite action plan by a Multi-Stakeholder Task Force that was formed as an outcome of the tripartite workshop “MFA and beyond”, held in Colombo in July 2004. The workshop was organized by the ILO at the request of some workers’ organizations and the Apparel Industry Labour Rights Movement (ALaRM), a consortium of workers’ organizations and NGOs which has been working on the issue of potential job losses associated with the end of quotas.

The tripartite action plan to deal with possible job losses as the TC industry restructures and adjusts to a post-MFA environment. Much remains to be done in terms of follow up and achieving the objectives of decent work.

The relationship between private systems of assessment and the MOL’s Labour Inspectorate

The number of labour inspections in general have declined over the last two years and with this the number of regular inspections within the zones have fallen. Thus the number of disputes over payment of statutory benefits to workers have been a major challenge.

The closure of factories within the zones have often happened abruptly and without adequate notice, and workers were left without compensation or back-pay and national insurance payments. For example, by the end of 2005, 15 factories had closed with over 3,000 workers losing their jobs. Only three factories paid any form of compensation to the workers; many others defaulted on employment protection payment. A more serious problem is the payment of Provident Funds.

In the vacuum created by the lack of regular labour inspections from the Ministry of Labour, many garment buyers and multinational enterprises – comprising 50 per cent of the total number of EPZ establishments – now implement a system in their supply chain through which their suppliers are assessed for conformity with a code of conduct. These assessments are also known as “social audits”. For example, Nike employs its own compliance officials in its factories. A large number of companies within the zones in the garment export trade have also recruited their own compliance officials who work together with the personnel department. One company visited in the Colombo EPZ paid US\$1,300 for each of five audits conducted by five different buyers during the past 12 months.

In this regard, for the MOL and the ILO, the following issues are raised: given that the ILO international instruments are most frequently cited in Codes of Conduct, what steps can be taken to put into practical effect the principles underpinning these international instruments to private enterprises; second, how can this be done in a manner consistent with the approach of the ILO as stated in

the instruments; and third, what is the relationship between these private systems of assessment and the MOL's labour inspectorate, and how can their activities be coordinated?

In response to a request by the apparel industry to discuss ways of ensuring the highest levels of compliance and give this sector a competitive edge, the ILO, in partnership with EFC and the Joint Apparel Associations Forum (JAAF), organized a Compliance Managers Conference which dealt with social auditing, compliance and labour issues. More work needs to be undertaken in working towards a multi-stakeholder monitoring mechanism with the participation of the MOL.

Facilitating the entry of labour inspectors in the FTZs

One of the key factors for effective inspections in the FTZs is the free entry of labour inspectors to undertake routine and surprise inspections. Sri Lanka has ratified ILO Convention 81, Article 12 of which enables labour inspectors to enter freely workplaces liable to inspection. Section 40 provides that “any employer who fails to permit entrance, hinders any officer in the exercise of the powers of inspection, fails or refuses to furnish such records, prevents any other person from answering an inspecting officer or furnishes false information shall be guilty of an offence punishable with a fine, a term of imprisonment or both”. Similar provisions regarding the power to enter and inspect conditions in workplaces pertaining to safety, health and welfare standards stipulated by law are found in the Factories Ordinance, which applies to a majority of the enterprises established under the BOI.²

It is important for labour inspectors to observe the confidentiality required with regard to the purpose of the inspection if it is carried out in response to a complaint, specifically as to the source of the complaint. According to the BOI, this issue has risen due to the security provisions necessitated by the EPZs being custom-bonded areas. Thus, they state that anyone entering the zone must have BOI permission by way of appropriate identification, to satisfy the customs and legal requirements on security. Consequently the position seems to be that while workplaces in the EPZs are not excluded from labour inspection, and as EPZs are high-security areas, access to such workplaces is subject to prior permissions. This is a major concern for effective compliance of labour laws given the increasing complaints regarding non payment towards provident fund and the trust fund.

To address the issue of entry into the zones, way back in 1999 the ILO Colombo Office brokered an agreement between the BOI and the MOL, resulting in an MOU between the two parties. One of the key points in the agreement was consensus to place an officer within the zones. Apparently this arrangement worked only in one zone and not in others. Most stakeholders agree that the ILO Colombo Office should convene a meeting to revisit this arrangement.

A new MOU needs to put in place new working modalities to gain access to workplaces in the EPZs without prior authorization. The provision of proper credentials is a requirement in Article 12 of the Convention which should enable inspectors, in practice, to enter freely and without previous notice any workplace

² This issue was discussed by the CEACR in June 2007 as a result of complaints by unions.

liable to inspection or which they may have caused to believe to be liable to inspection.

Targeting BOI factories outside the EPZs for labour inspections

At present, there are 300 BOI factories inside the FTZs and about 1,200 BOI establishments with the same conditions outside the zones.

The BOI Industrial Relations Department has in the past undertaken fairly regular monitoring of the 300 BOI factories inside the zone, but not the 1,200 outside. One of the constraints faced by industrial relations officials is understaffing and the lack of formal training in either dispute settlement or basic monitoring of labour standards and undertaking assessments as a preventive activity. The monitoring/assessment is usually undertaken by senior officials and any shortcomings found are communicated to MOL officials for necessary action.

Concerning the factories within the zones, the main activities of BOI IR officials can be summed up as follows:

- maintaining industrial peace by settling disputes;
- handling grievances and coordinating with the MOL when initial mediation fails;
- monitoring of labour standards through regular visits;
- facilitating the establishment of Employee Councils and promoting workplace cooperation.

Maintaining a Central Employment Data Bank to register job seekers and place them in suitable jobs. Naturally this had an effect on the BOI factories both inside and outside the bonded zones. Here the BOI industrial Relations officials also have a responsibility to monitor labour standards and work closely with their MOL counterparts.

The key issue for compliance with labour standards is that other 1,200 establishments outside the bonded area designated as BOI factories. The overall responsibility according to the BOI is with MOL which itself has seen a fall in regular inspection.

This situation of non-compliance in some EPZ factories regarding statutory dues, particularly Provident Fund benefits, has been compounded by the growth in outsourcing third-party contracts in the production chain. Some of these establishments outside the zones also act as suppliers for the larger factories inside the zones. It is therefore imperative that proper labour inspections be undertaken for the 1,200 factories on a priority basis.

Improving the planning, monitoring, and implementation of labour standards

Sri Lanka has ratified ILO Convention No. 81 on labour inspection and is thus obliged to maintain a system of inspection in order to secure the enforcement of laws relating to working conditions and the working environment, provide information and advice to employers and workers on how to comply with national laws, and ensure that defects or abuses not covered by existing laws are reported to the competent authority.

The Convention does not stipulate the precise details of the inspection system, other than that it should be under a central authority. In Sri Lanka the central authority is the Department of Labour within the Ministry of Labour. The Department is responsible for a number of divisions, each with responsibility for enforcement and compliance in different areas. The inspection of working conditions, work safety and occupational hygiene is undertaken by different inspectors. Sri Lanka has some 400 labour inspectors responsible for general inspection relating to working conditions under various legislations, and another 25 inspectors responsible for inspection under the factories legislation. In addition, the Employee Provident Fund has 200 officers (field officers) responsible solely for ensuring compliance under EPF legislation. In effect, therefore, inspection functions are undertaken by three different types of inspectors.

A modern labour inspection system is driven by the objectives of prevention, protection coordination and improvement, with the actual design of the inspection system a response to these objectives. Under such a system the emphasis is on securing compliance with all labour laws and regulations. With the assistance of the ILO, the MOL has lately been reorganized, the inspection form revised, and a monitoring and implementation unit set up. These efforts were expected to have a positive impact on the inspection system and increase the number of labour inspections (which has severely decreased from 2005 . Instead of the minimum 20 inspections per month per inspector, most labour inspectors were conducting inspections of only 50-60 per cent of the targeted establishments assigned to them).

It is recommended that the MOL inspectors, the OSH inspectors and the BOI officials coordinate their activities and work as a team, in tandem with the private sector audits which are on the increase. It is expected that the new National Institute of Occupational Safety and Health and the Institute of Labour Studies, although not having inspection duties, will be able to provide the required technical support for the successful operation of a well coordinated inspection system.

The proper management of the inspection system necessitates an approach to labour inspections that makes better use of inspection resources, including logistics, transport, etc. This will increase the effectiveness of routine inspection visits undertaken by inspectors (helping to prevent small issues from escalating into major problems).

The other major issue concerning labour inspections is how to work closely with trade unions and employers organizations and other stakeholders in securing compliance.

Computerising data on labour inspections undertaken in EPZs

Both the BOI and the MOL presently lack an effective mechanism for monitoring and analysing inspections of enterprises. The MOL's administrative and information processes in Sri Lanka have in the past relied heavily on manual procedures, resulting in a massive flow of paperwork pertaining to inspections. Data on compliance required by the Ministry of Industry or the BOI on the extension of GSP Plus status were also handled manually. It is now well recognized that that the manual, paper-intensive system is low in productivity, inefficient, and not consistent with a modern approach to labour administration.

To address this, it is highly recommended that a computerized system be put in place for the intake and analysis of data obtained during inspections. In early 2007 all the districts offices of the DOL acquired e-mail facility. Computerization will facilitate the planning of inspections and follow-up work, particularly the MOL's district and sub-district offices. The MOL's work on effective monitoring of the BOI factories will be greatly enhanced by computerisation. In this manner both the BOI and MOL will be able to tap into a common database.³

Increasing the number of skilled labour inspectors

With the expansion of the Sri Lankan economy, the number of enterprises liable to inspection also increases. In order to maintain and increase the quality inspection penetration rate within the zones, more and better trained inspectors will be needed.. This will also require shifting the emphasis to prevention and working closely with trade unions, employers and buyers and other civil society groups. As well, media and corporate communications campaigns could be launched to broadcast messages on non-compliance, productivity, and good practices to stakeholders on a large scale.

In the meeting with the Permanent Secretary, it was made known to us that MOL was in the process of recruiting 100 labour inspectors in the three months following. In this regard, it would be appropriate to review the required qualifications for inspectors and to ensure proper training for them in the task of securing compliance rather than policing enterprises.

Promoting social dialogue and the freedom of association in EPZs

The general complaints raised by most trade unions pertain to the difficulty in organizing and acquiring recognition in the free trade zones. This is due among other things to employers resorting to the creation of Employees' Councils (as promoted by the BOI) which have the effect of hampering the creation of free and independent trade unions and the exercise of the right to bargain collectively. The unions have already complained to the Committee on Freedom of Association (Case No. 2255, Complaint against the Government of Sri Lanka, presented by the International Textile, Garment and Leather Workers' Federation (ITGLWF) on behalf of the Ceylon Mercantile Industrial and General Workers' Union (CMU)).

Employees' Councils have been in existence since 1994. However in June 2002, at the time when Sri Lanka was applying for the GSP Plus status, the BOI published a set of revised standards called "Guidelines for the Formation and Operation of Employees' Councils". The unions point out that Employees' Councils are set up without consultation with the unions, and are under the control of the BOI which is able to actively participate in all aspects of the Councils' activities. They maintain that the Employees' Councils are not freely elected and are therefore not "elected representatives", as defined in the Workers' Representatives Convention, 1971 (No. 135), and that the control exerted by the BOI prevents the Employees' Councils from acting in full freedom to organize their activities, formulate programmes and promote effectively the interests of their

³ The ILO-DIALOGUE Better Factories Cambodian Project is currently reviewing the computerisation of garment factories. In Southern Africa, the ILLSA (Improving labour systems in SA) project has also developed a software programme for monitoring and evaluating labour inspections. So far the project has provided computerised systems to Namibia, Lesotho, and Swaziland

members. In addition, the BOI was seen as being clearly partial to the Employees' Councils over trade unions.

Finally, unions are of the view that the current procedures for recognition in the existing law are unsatisfactory. The BOI Guidelines state that if a union represents 40 per cent of the workforce, then the union – not the Employees' Council – can represent the workers in collective bargaining; however, if the union does not meet this minimum requirement, then the Council can become the collective bargaining agent if authorized by at least 40 per cent of the workforce. This has put unions and Employees' Councils in a position where they must compete for bargaining rights, which is a breach of the freedom of association.

Notwithstanding this, the unions are trying to develop a strategy for both the medium and long term on the issue of Employees' Councils. In the years before the end of the MFA in December 2004, the ILO Colombo Office played an active role in organizing activities in the garment sector to overcome the adverse effects associated with the end of MFA. The Apparel-industry Labour Rights Movement (ALaRM), a collective of trade unions, labour NGOs and observer organizations affiliated with the apparel industry, was formed during this time to work for the rights of women workers in the industry, specifically to train, educate and raise awareness of rights among women workers, study and publicize the working conditions of the workers in the garment industry, negotiate with the managers and owners of the garment factories to improve the welfare of women workers, and request the government and the buyers to act with responsibility on labour matters. At present, ALaRM is engaged in mobilizing workers, research and documentation, media and publicity campaigns, lobbying and negotiating with employers, the government and buyers – all part of an international campaign to improve the plight of workers.

Some of the unions in ALaRM have agreed that since only about 35 factories have registered trade unions, it may a good interim measure to work with Employees' Councils, as the latter can handle some of the grievances of the workers which are currently not being addressed at all. In addition, they maintain that working with Employees' Councils can lead to the formation of trade unions. They argue that this is one of the “new forms of organizing” in the labour movement that takes into consideration the changed nature of work, in the process enabling ALaRM to efficiently reach a large number of factories and mobilise their workers. In short, in the absence of any other workers' bodies at the enterprise level, the Employees' Councils can be used to advance the rights of workers and can be a good stepping stone for building a strong labour movement in the predominantly female apparel sector (interview ALaRM member, August 2007).

Other unions in ALaRM pointed out that the organization of trade unions has been unsuccessful due to several factors: suppression by the employers of unionization efforts, misinformation concerning trade unions, the government policy of non-implementation of laws relating to trade unions, and the lack of trade union capacity and financial resources to organize workers (interview with Marcus, August 2007). However, they add that the major issue within the FTZs, especially in apparel factories, was that the employers have used Employees' Councils against the attempts to unionize and that the Councils had been basically introduced in order to prevent the formation of trade unions.

However, they expressed willingness to work with Employees' Councils on the following conditions:

- Statements should be prepared and distributed among employees to create awareness about the real nature and workings of Employees' Councils.
- The differences between Employees' Councils and trade unions should be made clear in discussions with the members of Employees' Councils, with the participation of trade union representatives.
- Exchange programmes should be organized to allow union members to share their experiences with non-union workers in other enterprises in the EPZs.

By and large, unions are not happy with the progress made in organizing unions in Sri Lanka's export processing zones (EPZs), their complaint that employers often refused to recognize unions or bargain with them, leading to strikes and lock-outs.

The process of granting recognition to unions for collective bargaining purposes is marked by excessive delays. Employers tend to delay the holding of union certification polls for a long time, and many union members are harassed and/or fired in the meantime. As a result, workers are afraid of being identified with unions, especially when the union loses the poll. Employers also resort to outsourcing in order to alter their workforce figures to ensure that the 40 per cent union membership requirement is not met. The Department of Labour recently sought to address this problem by issuing instructions to labour officers on the implementation of the law and on pro-active measures to be taken to facilitate union certification polls.

According to the unions, the 1999 Industrial Disputes (Amendment) Act, which protects workers against acts of anti-union discrimination in taking up employment and in the course of employment, has not been effectively applied. They do not think that the maximum penalty of US\$250 is a strong enough deterrent. Since the Act was adopted, many serious cases of anti-union discrimination and non-recognition of trade unions have been reported.

The Labour Department is responsible for filing complaints against employers alleged to have engaged in unfair labour practices. Such offences are tried before a Magistrate's Court. Due to a backlog, it takes a long time to bring cases to court, and the delays lead to the weakening and disbandment of unions.

To summarize, in Sri Lanka the alliance between the unions and local NGOs enabled it to focus its agenda on promoting decent work in the EPZs and organizing the unorganized workers. ALaRM is in a position to enter into a dialogue with the stakeholders to promote collective bargaining and workers' rights. According to ALaRM, there are 35 unionised establishments in the EPZs and given the relatively low wages prevailing in the EPZs, the activities of ALaRM will go a long way in promoting collective agreements.

As the ITGLWF General Secretary Neil Kearney remarked:

... Key to sustainability is the establishment of mature systems of industrial relations built around social dialogue. "In the industrial context effective dialogue requires a voice for workers as well as management. Unfortunately, serious shortcomings in the application of the right of workers to freedom of association and to bargain collectively can make social dialogue almost ineffective. Increasingly, it is recognized that no matter how well intentioned the corporate social responsibility approach of brands and retailers, the impact is limited and unsustainable in the longer term without social dialogue. Given that social dialogue is a key outcome of unionisation and collective bargaining it is now essential that these be at the heart of any sustainable Decent Work programme in the EPZs in global value chains and CSR initiatives (Kearney, 2006).

The ILO is implementing a number of technical cooperation projects (Better Factories Cambodia, Better Work, Morocco Jordan decent work project in the garment industry), which promotes and facilitates dialogue between national social partners and buyers (multinationals). The ILO policy position is that no CSR (corporate social responsibility) initiative is sustainable unless it is connected to and supported by a strong national industrial relations system and its actors. CSR work is usually top-down, with the MNEs imposing social compliance on their trading partners. Recent studies conducted by the Ethical Trading Initiative (ETI) show that this “policing” approach is costly and does not result in positive changes in terms of social compliance. The ILO’s approach is to build a win-win partnership between national social partners and MNEs in EPZs to improve the industry’s competitiveness and compliance with national law and core international labour standards. Building sound industrial relations is vital in this strategy.

Employers’ initiatives to promote decent work in the FTZs through the Factory Improvement Programme

The Employers’ Federation of Ceylon (EFC) is the leading employers’ organization in the region. Currently it has a membership of almost 500 members, of which 78 are BOI establishments. Many of the garment factories in the zones are members of the Joint Apparel Association Forum (JAAF), an associate member of the EFC.

Under the Local Management Development Project, MCC and the Declaration the EFC collaborating on an intensive training and follow-up effort in both EPZ and non-EPZ enterprises, starting in Sri Lanka and gradually moving into other selected countries.

During the past four years, the EFC participated in a programme for the garment sector which increased labour productivity and product quality and promoted bipartite dialogue and safe working conditions. The Factory Improvement Programme (FIP) was implemented, with ILO support, for the apparel sector in the EPZs, designed to raise the factories’ capacity to comply with international labour standards and increase their competitiveness.

The programme comprises six training modules, followed by visits to the participating factories by the experts conducting the modules. The modules are as follow:

- (1) continuous improvement (setting in motion the structure, discipline, teamwork and commitment of senior management towards the entire project);
- (2) quality improvements (tools, techniques, systems and internalizing a quality culture);
- (3) workplace cooperation (introduce/enhance worker-management relations and social dialogue, participation of worker-level teams for a two-way process and worker rights);
- (4) productivity enhancement (process planning and monitoring, efficient techniques and overtime assessment and monitoring);
- (5) human resources management (organization culture, procedures and practices, payroll practices, employee appraisals and worker development);and

- (6) occupational safety and health (safety techniques, safety training, healthy workforce and conforming to international requirements).

Given the low productivity prevailing in most enterprises in the garment sector, there is a need for follow-up by the employers to ensure more garment factories come within this scheme (Best, 2005)

The programme methodology – in terms of targeting management capacity, combining labour issues with those of productivity and quality, and action-orientated learning – worked well in making the programme a success.

According to the EFC, the FIP can be credited for improvements in most factories (IOE, 2007). A major achievement was the introduction of improved management systems and better understanding of how to address labour issues on the part of the managers. The programme put in place straightforward changes, such as improved measuring and planning systems (mainly because the managers were most interested in these). Workers benefited from the changes in terms of higher wages and better health and safety conditions at work.

The modules on social dialogue, HR and continuous improvement also achieved positive changes; workers reported that communication between workers and managers had improved.

The discussions at the Employees' Councils were generally seen by workers as the platform for raising their concerns. Typical problems workers cited as being resolved through the Councils involved transport, canteen food and pay anomalies. Workers in some factories mentioned wider changes arising from the FIP, such as more comfortable working environments and improvements in productivity and quality. The quantitative data also show improved business performance between the programme start and end. In-line and end-of-line defect rates across all factories fell by an average of 25 per cent and 42 per cent respectively. The man-machine ratio fell by an average of 19 per cent and cost-per-minute by 12.5. Falls in labour turnover (34 per cent) and absenteeism (27 per cent) provide indirect evidence that improved people management can increase employee satisfaction and commitment. Managers believed these improvements had direct consequences for efficiency and cost control, e.g. through lower recruitment and induction costs and lower risks of production hold-up (due to lower absenteeism).

The EFC is convinced that this experience can be now transferred to the factories in the bonded area as well as to their 78 BOI members who are outside the zones. The EFC has set up a voluntary mediation centre and is keen to work with the newly formed Association for Conflict Resolution in preventing disputes. Both initiatives will be of importance to the promotion of sound industrial relations in Sri Lanka and within the EPZs.

Following the success of the FIP programme, the FIP methodology has been adapted in **Cambodia** (the Better Factories Project) as well as in Vietnam and India.

EPZs and social dialogue

The EPZs have been characterized by the lack of social dialogue between employers' and workers' representatives; higher level tripartite social dialogue at the National Labour Advisory Council (NLAC) regarding the zones has also been very limited.

The weak enforcement of labour laws and the intense production processes in the EPZs can create an environment that generates conflict. In the absence of adequate mechanisms and processes for information-sharing, consultation, negotiation and dispute settlement, many of these conflicts are inadequately addressed and channelled. This is further complicated by the fact that many zone enterprises are run by managers unfamiliar with local customs in the country.

All the issues pertaining to adjusting to a post-MFA era discussed above and the promotion of decent work require a workable system of social dialogue as the key element in a strategy to mobilize and develop the capacity of all three partners – employers’ and workers’ organizations and the government’s labour administration system – in order to improve employment conditions.

Recommendations

The Government of Sri Lanka is looking to the EPZs to make important contributions to development in terms of foreign exchange and employment generation. Apparel exports, which comprise a major chunk of total exports, successfully faced a quota-free trading environment during the last two years, but are likely to face intense competition in 2008 with the removal of restrictions on China’s exports to the U.S. market. Sri Lanka’s apparel industry needs to continue its efforts to enhance the quality of its products, improve compliance with international labour standards and with good governance principles, assure timely production and delivery, offer competitive pricing, improve the skills of its labour force, and the develop reputed international customer bases.

As well, continuing efforts to obtain some relief from the current Rules of Origin (ROO) criteria imposed under the GSP Plus scheme, which requires Sri Lanka to add at least 50 per cent value addition in case of apparel exports in order to be qualified for such benefit, would be highly beneficial (RCB, 2006) A better competition policy and a development framework for FDI are important, so is the need to focus on a decent work policy framework.

Given that the GSP Plus status will come up for review next year, it is vital for the key stakeholders and other actors concerned to work together to develop effective national policies that would fit into the DWCP (Decent Work Country Programme) of Sri Lanka. Such policies should promote decent work and foster investment and trade in the EPZs in the bonded area and in the 1,200 establishments outside the bonded area. The issues that must be addressed include compliance with labour standards, social dialogue between the stakeholders, productivity, investment and technological upgrading to enable enterprises to move up the value chain.

Today there are also voluntary approaches emerging in the global market, e.g., the Framework Agreements between Global Union Federations and multinational companies. While the content of these agreements differ, most cover the core international labour standards and some also address issues such as “living wage” and health and safety concerns.

Coordination between the labour inspectorate and the private system of assessment

The MOL, the BOI and the social partners need to jointly work out a coordination mechanism between the private systems of assessment (undertaken by global brands such as Nike and Gap) and the labour inspectorate to ensure consistency with the approach of the ILO. Initiated in 2004 at the initiative of the ILO Colombo Office, this process should be continued and boosted; the ILO's work in this area in other countries (Better Factories Cambodia, Better Work, Morocco Decent Work project in the garment industry, Jordan TC project, etc.) can be useful models. In these projects the ILO facilitates dialogue between national social partners and buyers (multinationals). For the CSR initiative in Sri Lanka to be sustainable, it has to be connected to and supported by strong national IR systems and its actors.

Promoting social dialogue in the EPZs

The issues presented above present challenges to the tripartite constituents in Sri Lanka to mobilize and work together to develop stronger partnerships and work towards extending the GSP Plus status. This will go a long way to ensure the sustainability of the EPZ strategy in Sri Lanka.

The EPZs are part of global production systems which have emerged largely along sectoral lines, each sector developing distinct characteristics in terms of the organization of global production and governance of global supply chains. This is clearly the case in the Sri Lankan garment sector which produces labour-intensive consumer goods (textiles, garments and footwear); the ILO can continue to assist the constituents in this area in by urging the existing National Labour Advisory Council to engage in dialogue on issues of common interest and to reach agreement on conclusions and recommendations for the improvement of social and economic conditions. Although the agreements that can be reached may be voluntary, they can have considerable influence in shaping policies and practices in specific sectors.

Employers

The employers' experience in implementing FIP 2 and 3 gives them a platform to improve competition, productivity and quality in the EPZs. The work done on a pilot basis in the FIP programmes in the last three years needs to be shared with their members: the 78 companies with BOI status, and JAAF (their major sector member). The EFC's excellent training department can assist companies in and outside the EPZs to improve working conditions and productivity through remediation and training, and by working with the government and international buyers to ensure a rigorous, transparent and continuous cycle of improvement. During our meeting with the EFC Director-General, the latter recommended that the ILO include this issue in their DWCP and secure funding to enable the employers to promote decent work in the EPZs through the FIP.

Strengthening the MOL's capacity to enforce labour laws and promote social dialogue

1. A major factor for effective inspections in FTZs is the free entry of labour inspectors to undertake routine and surprise inspections. The MOL and the BOI need to revisit the original MOU to ensure that labour inspectors are able to gain

access to workplaces in the EPZs without the need for prior authorization (in line with ILO Convention No. 81, ratified by Sri Lanka).

2. Strengthening the planning, programming and monitoring capacity of the MOL

As in most developing countries, the capacity of the Sri Lankan labour inspectorate needs to be improved. Although there are 400 labour officers, not all of them undertake inspection work. The Ministry's Monitoring Unit should be commended for the recent initiatives which have increased the number of inspections undertaken. These efforts need to be intensified to target the EPZs. Equally important is the training of inspectors and zonal managers on managing the inspection process.

There is a need for an inspection review in order to increase the frequency of public inspections in EPZ establishments in light of the upcoming GSP Plus review. The inspection review needs to take into account the frequency of private monitoring by buyers and identifying the gaps and overlaps.

Computerized information management system

One of the major tasks for the MOL is the development of a computerized information management system (IMS), similar to those found in Singapore, Hong Kong, Malaysia and Cambodia (under the Better Factories Programme) and the work carried out in the ILLSA project by the CTA. The ILO Colombo Office may be able to assist in a pilot phase to computerise the data on inspections from the 1,500 establishments. In this regard, the recommendations already put forward by a consultant regarding software should be taken into account. The MOL is eyeing the developments in the ILLSA project in Southern Africa whose ILO-developed software could be shared with the Sri Lankan MOL.

The MOL can also use the media as an effective means of disseminating information on labour law and good practices. Technological developments such as the Internet and low-cost delivery systems for television and radio have increased the quantity and range of information that can be made available to workers and employers, even to remote areas where the BOI factories are located. It is suggested that the public relations unit of the MOL look into this recommendation.

The MOL also needs to review the existing social dialogue mechanisms within the National Labour Advisory Council with a view to facilitating debate on promoting decent work in the EPZs. It is recommended that a subcommittee be created to discuss the labour issues in EPZs on a regular basis. Best practices and lessons learned from other countries also show that engagement with all stakeholders – including government agencies, workers' representatives and unions, factory owners, and civil society – is a necessary component of a strategy to promote decent work in EPZs.

Review of labour law

To promote collective bargaining in the FTZs, the government needs to review the legal provisions concerning the recognition of trade unions and penalties for unfair labour practices, as existing fines are too low. As outsourcing and employment relationships have emerged as a major issue, the constituents have urged the MOL to organize (with the assistance from the ILO) a tripartite workshop on ILO Recommendation No. 198.

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