



Action Report Social (Human Rights)

Gap
April 25, 2012

Ticker	Exchange	Meeting Date	Record Date	Annual Meeting Location
GPS	NYSE	5-15-12	3-19-12	San Francisco, California

Agenda

Item	Proposal
1	MGT: Elect directors
2	MGT: Ratify selection of auditors
3	MGT: Shareholder advisory vote on executive compensation
4	SH: End trade with Sri Lanka

Si2 Briefing [Social \(Human Rights\)](#)

Report Author [Peter DeSimone](#)

Links [Proxy Statement](#); [10-K Filing](#)

Resolved Clause RESOLVED: We, as shareholders of Gap Inc., request that the Board institute phased procedures for Gap Inc. to end trade partnerships with Sri Lanka, until the Government of Sri Lanka ceases human rights violations.

Lead Proponent Stephen Jaeger

Vote History The company successfully challenged the proposal at the Securities and Exchange Commission (SEC) last year, arguing it was submitted too late. However, Gap lost at the SEC this year. It argued the resolution could be omitted because it contained false and misleading statements, related to less than 5 percent of Gap's business and concerned ordinary business. The SEC disagreed on all points.

Summary Stephen Jaeger is treasurer of the International Tamil Technical Professional Organization, a non-profit group which says it aims to help in the "development of the war-torn Northeast Sri Lanka." He has concerns that Gap's business ties in the form of supply contracts for the manufacture of its branded apparel pose reputational risks for the company and its shareholders. He points to the Sri Lankan government's dismal human rights record, as well as the widespread reports of human rights abuses in Sri Lanka, especially against women and ethnic minorities. From a reputational risk standpoint he believes Gap should stop doing business in Sri Lanka until the government reforms.

Gap says it shares Jaeger's concerns but feels that workers in Sri Lanka are much better off for its business presence there. It notes it upholds a code of conduct that, among other areas, ensures its suppliers comply with internationally recognized human rights standards. It says its code and monitoring efforts also help ensure the Tamil minority

and women in Sri Lanka—two groups considered to be at risk by human rights groups—are not discriminated against in employment in its suppliers’ factories. Gap also notes its many philanthropic programs aimed at promoting positive change and human rights as evidence that its activities in the country are doing more good than harm. Therefore, Gap says, it believes its presence in Sri Lanka is doing more to promote human rights than its exit from the country ever could, and it is asking shareholders to vote against the proponent’s resolution.

I. Gap and Human Rights in Sri Lanka

Founded in 1969, Gap is a global specialty retailer, offering apparel, accessories and personal care products for men, women, children and babies under the following names:

Financials			
(\$ millions)	2010	2011	% Change
Total Revenue	\$14,664	\$14,549	(0.8%)
Net Income	\$1,204	\$833	(30.8%)

- **Gap**—The company’s flagship brand sells apparel for men and women influenced by its American roots. In addition to designing merchandise, Gap offers limited-run collections in partnership with well-known fashion designers and other third-party merchandise. Gap began selling children’s apparel in its GapKids stores in 1986 and expanded to babyGap in 1989. It later added maternity apparel and Gap-Body—a line of lounge and sleep wear, intimates and active apparel for women. Gap’s price points are set between its more upscale Banana Republic brand and its more moderately-priced Old Navy collection, described below.
- **Banana Republic**—Acquired in 1983, this is a multi-channel brand offering work wear for men and women, including apparel, handbags, shoes, jewelry, personal care products and eyewear.
- **Old Navy**—Launched by Gap in 1994, it offers value-priced apparel, shoes and accessories for adults, children and babies, as well as a maternity line.
- **Piperlime**—Created by the company in 2006, it is an online boutique that sells a mix of private label and third-party brands in footwear, apparel and accessories for women and men, as well as footwear for kids.
- **Athleta**—Acquired in September 2008, this is Gap’s newest brand and markets women’s sports and active apparel and footwear for a variety of activities, including golf, running, skiing, snowboarding, tennis, swimming and yoga.

Gap has company-operated stores in the United States, Canada, the United Kingdom, France, Ireland, Japan, China and Italy, as well as franchise agreements with unaffiliated franchisees to operate Gap and Banana Republic stores in Asia, Australia, Eastern Europe, Latin America, the Middle East and Africa. It has more than tripled its franchise store base from the end of fiscal 2007 to 227 stores at the end of its 2011 fiscal year. Gap’s products also are available to customers online in more than 90 countries through the company’s websites and using a U.S.-based, third-party logistics and fulfillment firm. Gap ended its 2011 fiscal year with 3,263 company-operated and franchise stores.

Sourcing: Gap designs almost all of the products it sells, but outsources manufacturing of them to third parties worldwide. It is this supply chain that has raised concerns for human rights activists over the past two decades and it is the target of the proponent’s proposal on ending business ties to Sri Lanka.

Financing: In addition, the Gap, Banana Republic and Old Navy brands each have private label and a co-branded credit card programs, managed by a third-party financing company.

2011 financial performance: The iconic Gap brand continued to suffer declines in same-store sales in 2011 due to weakening popularity and the moribund economy in its U.S. home market, as reflected in its decreasing revenues and net income between 2010 and 2011. Its fiscal year 2011 comparable sales, including online sales, were down 4 percent compared with a 2 percent increase in 2010. Still, Gap pointed to progress in implementing its long-term strategic plan to turn around its brands in the United States and to grow its online and international businesses. In 2011, Gap grew sales in its online division by 20 percent and in its franchise business by 45 percent.

Employees: As of January 28, 2012, Gap had approximately 132,000 part- and full-time employees. It also hires seasonal employees, primarily during the peak end-of-year holiday period.¹

Human Rights Concerns in Sri Lanka

Sri Lanka continues to witness widespread human rights abuses despite the end of the civil war there in 2009, a conflict that spanned nearly 30 years. The conflict's legacy raises especially serious concerns for the people collectively known as the Tamils, an ethnic minority comprising about 18 percent of the population. Muslims, who make up approximately 7 percent of the population and represent three sub-groups—the Sri Lankan Moors, the Indian Moors and the Malays, each with its own history and traditions—are another persecuted minority. Violations of women's basic human rights and widespread child labor also continue to be problems in Sri Lanka.

U.S. State Department: The U.S. Department of State's [2010 report on Sri Lanka](#) (released in April 2011) notes that President Mahinda Rajapaksa was reelected to a second six-year term in January 2011; his family dominates the government.² Although there is an independent parliament that was elected in April 2011, two of the president's brothers hold key executive branch posts as defense secretary and minister of economic development, while a third brother is the speaker of parliament. Independent observers, the State Department says, "generally characterized the presidential and parliamentary elections as problematic" and "fraught with violations of the election law by all major parties." It also notes the government continued to perpetrate human rights abuses on its people, and its security forces committed arbitrary and unlawful killings, although the number of extrajudicial killings declined in 2010. While Sri Lanka is definitely seeing more peaceful times, the State Department says, "repercussions of the nearly 30-year war against the Liberation Tigers of Tamil Eelam (LTTE) continued to have an effect on human rights, despite the defeat of the LTTE in May 2009." The report also notes that the Sri Lankan government continued to crack down on civil society organizations reporting human rights abuses.

Workplace issues: The U.S. State Department also reported widespread violations of workers' rights in Sri Lanka. Among the chief concerns raised by the State Department were discrimination against women and the ethnic Tamil minority. It also notes discrimination against persons with disabilities, as well as those living with HIV/AIDS, in addition to discrimination based on a person's actual or perceived sexual orientation. Other problems included widespread human trafficking and incidents of child and forced labor, although the State Department gives the Sri Lankan credit with instating new laws and funding to try to eliminate the persistent child labor problem.

Civil society assessments: Freedom House rates Sri Lanka as "partly free," citing many of the same issues as the U.S. State Department, and Human Rights Watch (HRW) offered a very similar evaluation in its latest annual report. HRW says that the government has "failed to conduct credible investigations

¹ Additional information on Gap's businesses and financial performance is available in its 2011 10-K statement, available at <http://investors.gapinc.com/phoenix.zhtml?c=111302&p=irol-SECText&TEXT=aHR0cDovL2lyLmludC53ZXN0bGF3YnVzaW5lc3MuY29tL2RvY3VtZW50L3YxLzAwMDEwOTMxMjUtMTItMTMyMDk4L3htbA%3d%3d>.

² U.S. Department of State. (April 8, 2011). *2010 Human Rights Report: Sri Lanka*. Retrieved from <http://www.state.gov/j/drl/rls/hrrpt/2010/sca/154486.htm>.

into alleged war crimes by security forces, dismissing the overwhelming body of evidence as LTTE propaganda.” It said the “government’s Lessons Learnt and Reconciliation Commission (LLRC), characterized as a national accountability mechanism, is deeply flawed, does not meet international standards for such commissions, and has failed to systematically inquire into alleged abuses.” While the government permitted emergency regulation, which has been active for nearly three decades, to lapse in August, HRW says, the government maintained “overbroad detention powers,” and “several thousand detainees continue to be held without trial, in violation of international law.”

Meanwhile, Amnesty International, in a report to the Office of the United Nations High Commissioner for Human Rights’ Committee Against Torture (CAT), characterizes a situation rife with human rights abuses.³ It highlights allegations of detainees being held arbitrarily for prolonged periods—sometimes years—without charge. “Many are arrested and detained on suspicion of links to the LTTE pending investigation and interrogation by Sri Lanka’s intelligence and security forces, or for what the Sri Lankan authorities have termed rehabilitation,” Amnesty International notes. However, “People alleged to be involved with the LTTE are rarely brought to trial,” and “Most of these detainees are eventually released for lack of evidence.” Therefore, Amnesty International says, it “is concerned at the routine use by Sri Lankan authorities of prolonged administrative detention to circumvent ordinary procedures” in contravention of international and Sri Lankan law. “Some detainees report being tortured and beaten by military personnel and paramilitary cadres working with government forces, such as the army and navy; by police, by inmates and by prison guards,” Amnesty notes.

In addition, Amnesty in its investigations found evidence of forced disappearances and bodies of victims of extrajudicial killings that often show evidence of torture. Furthermore, Amnesty International says, there are continued widespread concerns of gender based violence including violence amounting to torture, and the Sri Lankan authorities are not taking the problem seriously. Sexual violence in Sri Lanka is highly underreported, Amnesty says, and poorly investigated even when reported. Amnesty concludes, “Most perpetrators of human rights violations, including of torture, enjoy impunity,” because “There has been a consistent failure of the authorities to ensure that allegations of torture and other serious violations of human rights are investigated and that those responsible are brought to justice.”

UN special report: United Nations Secretary-General Ban Ki-moon released a [report](#) by a panel of experts in March 2011 concluding that both government forces and the LTTE conducted military operations “with flagrant disregard for the protection, rights, welfare and lives of civilians and failed to respect the norms of international law.”⁴ Among the credible allegations the experts found were cases of the LTTE in the final stages of the war:

- Using civilians as human shields.
- Killing civilians attempting to flee LTTE control.
- Using military equipment in close proximity to civilians.
- Forcing children to join the armed forces.
- Forcing civilians into slave labor.
- Killing civilians through suicide attacks.

³ Amnesty International. (October 2011). *Sri Lanka: Briefing to Committee Against Torture*. Retrieved from: <http://www.amnesty.org/en/library/asset/ASA37/016/2011/en/2bb1bbe4-8ba5-4f37-82d0-70cbfec5bb2d/asa370162011en.pdf>.

⁴ United Nations. (March 31, 2011). *Report of the Secretary General’s Panel of Experts on Accountability in Sri Lanka*. Retrieved from http://www.un.org/News/dh/infocus/Sri_Lanka/POE_Report_Full.pdf.

The panel recommended an international investigative mechanism be established to address grievances. It notes that Sri Lanka is party to the *Convention against Torture and Other Cruel, Inhuman or Degrading Treatment or Punishment*, among other international conventions on human rights that require it to report to UN bodies periodically on its compliance with these international norms, something the experts found Sri Lanka had failed to do in light of the allegations.

U.S. Senate Resolution 84: On March 1, 2011, the U.S. Senate passed a resolution calling on the Sri Lankan government to:

- Work with the international community to “establish an independent international accountability mechanism to look into reports of war crimes, crimes against humanity, and other human rights violations committed by both sides during and after the war in Sri Lanka and to make recommendations regarding accountability.”
- “Allow humanitarian organizations, aid agencies, journalists, and international human rights groups greater freedom of movement, including in internally-displaced persons camps.”

The resolution also requests that the President of the United States “develop a comprehensive policy towards Sri Lanka that reflects United States interests, including respect for human rights, democracy and the rule of law, economic interests, and security interests.”⁵ The U.S. Department of State has been reporting back to the Senate on the President’s efforts in this regard.⁶

Gap’s Human Rights Policies

Gap has had a supplier code since the sweatshop debate ignited in the United States and it was among the first retail companies to adopt such a code in 1996. It later adopted a human rights policy to better explain its expectations for its employees and vendors in 2010. Both policies are described below.

Supplier code: Gap’s *Code of Vendor Conduct* also has an associated vendor compliance program that includes an initial approval evaluation, ongoing monitoring and ratings, remediation when necessary, and cooperation on capacity building.⁷ Gap has a dedicated team of social responsibility specialists who work with the factories it monitors to ensure its code is enforced. In addition to checking compliance items, Gap’s specialists endeavor to gain the trust of workers and factory owners to understand how a factory operates and to improve working conditions. The specialists also assign ratings to factories used by the company’s buyers in making contract decisions and, in some cases, preventing Gap buyers from engaging a facility based on current conditions or prior conduct. In 2010, Gap’s specialists conducted more than 2,500 audits on more than 1,200 facilities that make its branded products.

Standards—The code has standards covering a broad array of legal compliance and environmental issues, in addition to core labor and human rights topics. On the human rights issue raised by the proponent’s proposal, the code sets standards on:

- **Child labor**—Gap bans child labor in its factories and calls for all workers in its suppliers’ facilities to be of legal age to work or at least 15 years old, whichever is the higher minimum.
- **Forced labor**—Gap prohibits use of all forms of involuntary labor, including prison labor, debt bondage or forced labor by governments.

⁵ See <http://thomas.loc.gov/cgi-bin/query/z?c112:S.RES.84.>

⁶ See <http://www.state.gov/j/gcj/srilanka/releases/187409.htm>.

⁷ See http://www.gapinc.com/content/dam/csr/documents/COVC_070909.pdf for a copy of Gap’s vendor code and <http://www.gapinc.com/content/csr/html/Goals/supplychain.html> for an explanation of its supplier compliance program.

- **Discrimination**—The code bars discrimination in all aspects of employment based on race, color, gender, nationality, religion, age, maternity, marital status, indigenous status, social origin, disability, sexual orientation, membership in workers’ organizations such as unions, or political affiliation.
- **Freedom of association**—Gap requires vendors to preserve workers’ rights to join associations of their choosing and to associate, organize and bargain collectively, as long as that activity is peaceful and lawful. It also requires factories in countries like China, where it is unlawful to form free trade unions, to find parallel means for independent and free association and collective bargaining.
- **Harassment**—Gap’s code forbids mental and physical coercion, including corporal punishment, and non-physical forms of harassments, including threats of violence, sexual harassment, screaming or other verbal abuse.

The code also covers standards for foreign contract laborers.

Better Work program—Gap also is a founding member of the International Labor Organization (ILO) and International Finance Corporation (IFC) [Better Work program](#), which operated in seven countries as of the end of 2011. As part of the program, participating Gap suppliers are monitored by the Better Work program instead of Gap employees.⁸ Gap then rates the suppliers based on the Better Work program’s findings and implements remediation programs as necessary. The program offers Gap stakeholders further assurances of factory conditions from a reputable third party.

Ratings—As noted earlier, Gap’s compliance program assigns one of four ratings—dark green (excellent), light green (good), yellow (fair) and red (action required)—to each factory it inspects, including factories undergoing a preliminary audit where it hasn’t done business yet. Its recent reporting demonstrates incremental improvement between 2009 and 2010, although approximately 16.7 percent of its vendor’s facilities continue to need immediate action on violations of its code. Gap suppliers in South Asia, where Sri Lanka sits, perform worse than average with 23 percent in this region needing immediate attention due to code violations. (See chart.⁹)

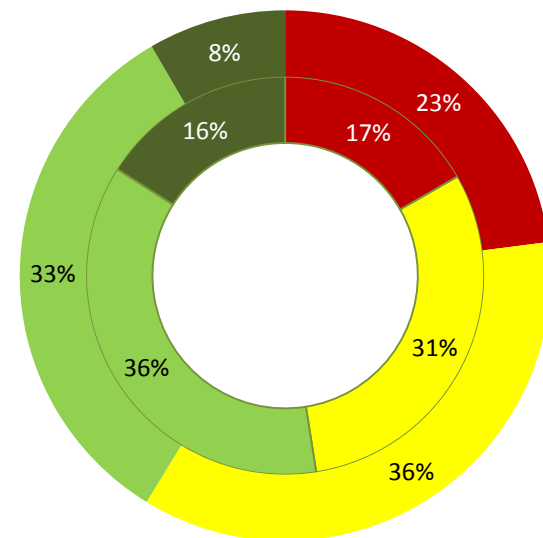
Human rights policy: Gap adopted a [Human Rights Policy](#) in 2010, which

Gap 2010 Factory Ratings (percent)

Outer Ring = Worldwide

Inner Ring = South Asia

■ Action required ■ Fair ■ Good ■ Excellent



⁸ See http://www.gapinc.com/content/csr/html/Goals/supplychain/our_program_in_action/ilo_ifc_better_work_program.html.

⁹ See http://www.gapinc.com/content/csr/html/Goals/supplychain/data/factory_ratings_by_geographic_region.html.

applies to its company-owned operations as well as to its supply chain.¹⁰ The policy is intended to augment its existing vendor code and highlight Gap's commitment to respect fundamental human rights, as embodied by international covenants such as the United Nation's *Universal Declaration of Human Rights*. The policy describes spheres of influence. Gap believes it has greater influence over working conditions in its operations and those of its suppliers, and less influence over prevailing industry, country and international human rights conditions. As part of this process, it has identified both geographic regions (areas where it sources branded products) and specific human rights issues—namely the core ILO conventions on child and forced labor, discrimination and freedom of association—where it sees the greatest need for its involvement and potential to effect change.

Gap's Business Ties to Sri Lanka

Gap does not discuss Sri Lanka in its [2011 10-K filing](#) or annual report. Reporting statistics from its vendor code compliance program indicate that it had 378 factories in South Asia in 2010, but a further breakdown of statistics on Sri Lanka is not available. (Human rights issues with these factories are discussed above.) Gap also does not disclose the volume or proportion of goods it sources from Sri Lanka or the risks it views from sourcing there. It is clear from its response to the proponent that it has a significant enough volume of sourcing there to employ a full-time human rights monitor there. It also operates several community programs in Sri Lanka. These are described under the heading "Management's Position" below.

Gap also discusses in its sustainability reporting on its website that it is monitoring the situation in Sri Lanka and that it will "carefully consider recommendations made by the U.S. government, the EU, the United Nations, and other appropriate international bodies that provide guidance on how apparel companies can play a positive role in bringing lasting peace to Sri Lanka." Gap adds:

The conflict in Sri Lanka has been particularly hard on working Sri Lankans of all backgrounds, and based on expert consultations, we feel that one of the most meaningful contributions we can make to help improve the overall environment in Sri Lanka is by providing safe and fair working conditions to individuals regardless of political affiliation or ethnicity. This is particularly true because apparel production is an important and much needed source of jobs in the country.¹¹

Gap also notes that in Sri Lanka it has a full-time local employee dedicated to ensuring that its workplace standards are being upheld.

[Brandix](#), one of Gap's reported vendors in Sri Lanka, posts a code with human and labor rights principles aligned with Gap's code, as well as a sustainability report. Brandix also has endorsed the UN Global Compact, which requires adherence to the internationally recognized human rights principles required by Gap. It reports passing inspections by the Worldwide Responsible Apparel Production (WRAP) organization, a non-profit assisting apparel and footwear manufacturers with supplier compliance programs. It also dedicates portions of its website to discuss the three key workplace concerns raised by human rights organizations: discrimination against women and the ethnic Tamil minority, as well as child and forced labor.

II. Proponent Position

The proponent notes that by the end of the long-standing civil war in Sri Lanka in 2009, some 40,000 Tamil civilians were killed and a further 300,000 interned in military camps and subjected to torture, rape and extrajudicial executions, in direct violation of international humanitarian law. He points to the

¹⁰ See http://www.gapinc.com/content/dam/csr/documents/HumanRightsPolicy_FINAL.pdf.

¹¹ See http://www.gapinc.com/content/csr/html/Goals/supplychain/our_program_in_action/sri_lanka.html.

United Nations Secretary General's panel of experts report on Sri Lanka, which found credible allegations of war crimes and crimes against humanity. These and other allegations are being further investigated and assessed by the UN Human Rights Council in Geneva, he notes. In addition, he cites a documentary of these mass atrocities by Channel 4 News in the United Kingdom as further evidence of human rights concerns.

Meanwhile, the proponent says, Sri Lanka's government-appointed Lessons Learned and Reconciliation Commission has failed to provide accountability. He quotes reports in 2011 from Amnesty International and other respected human rights organizations that "raise grave allegations of on-going human rights violations in Sri Lanka." Furthermore, he says, the U.S. Senate unanimously passed Resolution 84, "calling for measures for lasting peace in Sri Lanka," and the U.S. Senate's Committees on Appropriations "has proposed that international institutions vote against any loan, agreement or other financial support (except humanitarian aid) for Sri Lanka unless it complies with standards set by international law."

Notwithstanding these concerns, he says, the "Sri Lankan government's position of impunity continues to empower manufacturers such as Brandix, a major supplier of Gap...to expand its operations in Sri Lanka." The proponent says he is concerned that this could hurt Gap's reputation, especially considering Gap is one of the largest exporters of apparel from Sri Lanka, as it could be construed as an endorsement of the Sri Lankan government. In addition, Gap is indirectly bankrolling the government by fuelling economic growth and tax revenues through its buying activities there, which, the proponent says, keeps the government's "massive military viable." The proponent warns of continuing bad press for Gap for its ties to Sri Lanka, as well as consumer protests and boycotts, reputational blows, hurt employee morale and an overall erosion of brand value, spelling unwanted consequences for Gap and its shareholders.

The proponent believes Gap should not be supporting economic development in a country like Sri Lanka where the government routinely commits human rights abuses, especially considering that there are "ample alternatives for Gap...to temporarily move its manufacturing base to other cost-effective regions that pose no such threat." Therefore, the proponent is asking Gap to end all trade ties to Sri Lanka until the government there ceases committing human rights violations. In addition to preventing investments in Sri Lanka, the proposal also "calls for corrective actions to address existing investments in other countries that are associated with violations of human rights."

III. Management Position

Gap says its "shares the proponents' concerns for the protection of human rights and is committed to advancing the rights of garment workers around the world" and "understands the seriousness of the human rights allegations regarding the actions of the Sri Lankan government related to the past conflict and its aftermath." But it opposes the resolution because it believes its presence in Sri Lanka is helping promote respect for human rights there. At the same time, it says, while it does "not engage in a trade partnership with the Sri Lankan government," it is monitoring "steps being taken by the United States Government, the European Union and the United Nations" and believes "these are the best institutions to be engaging with the Sri Lankan government at this time."

In explaining its position, Gap says that "apparel production is an important source of much needed employment for Sri Lankans, whether they are Tamil, Sinhalese or others." It notes that in monitoring its suppliers in Sri Lanka it pays "particularly close attention...to the possibility of discrimination based on ethnic, religious, gender, caste or social status, especially in light of the past conflict" and works to ensure "safe, non-discriminatory and fair conditions" in those factories. It says "ensuring fair and equitable working conditions is one of the most important contributions we can make to help improve the overall environment in Sri Lanka." While it does not own production facilities in Sri Lanka or anywhere

else in the world and does not own stores or other operations in Sri Lanka, Gap notes that its suppliers to maintain contracts with the company must adhere to its Code of Vendor Conduct, which is aligned with internationally recognized standards of human rights, including the International Labor Organization's core conventions and the United Nations' *Universal Declaration of Human Rights*. Furthermore, Gap notes, it introduced a *Human Rights Policy* in 2010 that reinforces its existing vendor standards "to help ensure that workers who manufacture our products are treated fairly and with respect. (The vendor code and human rights policy are reviewed earlier in this report.)

To ensure its suppliers adhere to its policies, Gap notes, it employs "a global team that conducts regular announced and unannounced visits to factories with which we contract to verify that our garments are produced in an ethical manner." In Sri Lanka, it notes, it has "a full-time local employee dedicated to ensuring that our workplace standards are being upheld." It notes that its global team members speak the local languages, understand the cultures, have deep experience in this work and respect the confidentiality of workers communicating with them.

Furthermore, Gap says, its vendors make contributions to the communities where they operate. It notes its vendors in Sri Lanka contribute to "various initiatives to assist refugees and have set up additional factories to provide employment opportunities to the Tamil people." For example, Gap points out, it is working in central Sri Lanka with factories that employ up to a 40 percent Tamil workforce.

Gap also has been an active philanthropist in Sri Lanka since 2004, it notes, including:

- Contributing to a partnership with the Ceylon Chamber of Commerce that enabled 70 female entrepreneurs to rebuild their businesses in the Galle District following the 2004 tsunami there.
- Funding of 20 mobile desalination plants along the coastal belt, following the tsunami.
- Rebuilding of the maternity ward at the Dehiattakandiya Base Hospital in Ampara District, Eastern Province.
- Rebuilding of basic infrastructure facilities, including sanitation facilities, installation of tube wells to provide clean drinking water and facility renovations at schools in Dhambarawa and Mahiyanganaya in Badulla District, Central Province.
- Building a Water Resource Research & Training Center for water conservation and management in Anuradhapura, North Central Province, in partnership with a Sri Lankan manufacturer.
- Offering life and technical skills training and education in Tamil and Sinhala to female garment workers in Sri Lanka since 2009 through its Personal Advancement and Career Enhancement (PACE) program. Approximately 550 workers are participating in the program, and Gap plans to expand it further this year.

In these ways, Gap believes it is acting as a promoter of human rights in Sri Lanka, and it feels its departure from sourcing in Sri Lanka would do far more harm than good. Therefore, it is asking shareholders to vote against this proposal.

IV. Analysis

Key Points at Issue

- Would Gap and its shareholders benefit from ending trade ties to Sri Lanka?
- What would be the consequences for workers at Gap vendor factories in Sri Lanka if Gap left?
- Would Gap's exit prompt the Sri Lankan government to take further responsibility to improve its human rights record?

Disinvestment: Whether to disinvest from or otherwise stop doing business in a country because of its government’s human rights practices has been a debate spanning decades. Many point to the South Africa anti-apartheid movement as an example of a successful disinvestment campaign. In South Africa, however, there were calls for companies both to stay and promote positive change from within—by eliminating workplace racial discrimination, training black employees to advance in the company’s ranks, investing in schools and other social investment projects in local communities, and pressuring the government to change—and to disinvest and leave the country. Proponents of disinvestment, who were eventually in the majority, argued it was the only way to send a strong message to the government that apartheid would no longer be tolerated by the global community. Although the divestment movement, among many other factors, was eventually successfully in bringing an end to apartheid, the lives of many workers at U.S. and other multinational companies were dramatically affected by the parent company’s exit from the country, although hopefully positively benefited in the end with the advent of non-racial democracy in South Africa.

Disinvestment and ending trade ties also has been the call from human rights advocates and the general trend in dealing with the military junta in Burma (Myanmar). Pressure during the 1990s prompted many retailers to stop doing business there. While the jury’s still out on the regime, recent overtures by the Burmese government to inch toward democracy have many skeptical but hopeful that change is coming soon.

By contrast, human rights groups have long lamented multinational firms’ ties to the People’s Republic of China, but any calls for ending business ties have been quickly squashed by the country’s importance in the global economy. In turn, human rights groups have focused on persuading companies like Gap to improve their conduct and use their influence to promote change there.

Stakes for the company: With sufficient lead time, Gap could disentangle itself from contracts with Sri Lankan suppliers and stop doing business there with little financial consequences to the company. However, an abrupt pullout would have operational and financial consequences for Gap and its shareholders and could limit selections at its stores, which would hurt sales. Lead times for runs of collections are in many cases in excess of six months, so any orderly pullout would have to be completed over the course of a year. Still, without direct knowledge of the terms of the contracts Gap has in Sri Lanka, it is difficult to put a precise timeframe or price tag on the costs to Gap for ending business ties there.

There are also trade implications for Gap. Sri Lanka’s exports to the European Union (EU) qualified for duty-free entry under the EU Generalized System of Preferences (GSP) Plus market access program, granted in 2005 to help Sri Lanka rebuild after the 2004 tsunami. However, after a lengthy review process, the European Union suspended the GSP Plus market access benefit in August 2010, due to Sri Lanka’s poor human rights record. Sri Lanka continues to receive limited tariff preferences under the EU GSP program, and the country continues to receive preferential access to the U.S. market under the U.S. GSP program. However, if human rights concerns persist, it could prompt the EU, the United States or other key markets to pull access and implement sanctions, which is a policy area Gap and its shareholders will have to watch.¹²

Then, there is reputation to consider. So far, there have been no sweeping boycott campaigns calling on retailers to stop doing business in Sri Lanka. However, if a consumer boycott gained traction it could have reputational consequences for Gap. At the same time, Gap could brand itself as a responsible corporate citizen for avoiding Sri Lanka, although it would have to make its case and educate the public on the issue at the same time.

¹² Based on background notes from the U.S. Department of State last updated on April 6, 2011. Retrieved from <http://www.state.gov/r/pa/ei/bgn/5249.htm#econ>.

Another area to watch is if a Gap supplier in Sri Lanka would run afoul of the company's code in an egregious enough area to spark attention and consumer discontent with Gap's record. Shareholders should note, as outlined in the pie chart earlier in this report, that Gap supplier factories in South Asia, which includes Sri Lanka, perform worse in complying with Gap's code than the global average. At the same time, Gap has demonstrated a good record in dealing with such controversies as they arise and put its compliance program and other resources to task to fix the problem.

Consequences for the workers in Sri Lanka: The effects a Gap withdrawal from Sri Lanka would have on workers there is a much larger question. Jobs in the export sector in most developing companies tend to be better paying and often offer far better working conditions than most, even in cases where factories are still violating code commitments. If another buyer did not absorb the slack in the supply chain from a Gap departure from Sri Lanka, and it is likely that other buyers wouldn't take up all of the capacity left, workers are likely to lose jobs. In addition, Gap is among the more responsible retailers and buyers in the marketplace, with a human rights code and compliance program. It is possible that other, less responsible buyers would take up capacity in plants producing for Gap with less favorable contract terms and standards, and therefore potentially deteriorating conditions for workers. In addition, Gap supports several philanthropic programs in Sri Lanka that would likely suffer if it were to leave.

Influence on the government: Whether Gap's announcement that it was leaving would prompt the Sri Lankan government to take action would depend on its effects on employment and tax receipts and the willingness of other firms to fill the void. A unilateral pullout by Gap likely would have very little effect on swaying the Sri Lankan government. However, if Gap's move was matched by other apparel and footwear firms, it could make a statement that could force the Sri Lankan government to take notice. Apparel and footwear manufacturing is the second largest component of Sri Lanka's industrial sector and among the top contributors to gross domestic product in Sri Lanka, as well as a top export earner for the country, according to the U.S. State Department.

(Additional information on Sri Lanka, divestment campaigns and the human rights standards discussed in this report can be found in Si2's Briefing Paper [Social \(Human Rights\)](#).)

Voting Considerations

Voting for: Shareholders who feel that Gap should stop doing business in Sri Lanka on moral grounds and believe a Gap announcement of withdrawing from the country over its human rights record would help influence the Sri Lankan government to reform its human rights record will vote for this proposal. Others who have concerns for Gap's reputation in continuing to do business there during a time when human rights concerns persist in the country also may vote for this proposal, as will those who believe Gap could differentiate itself from its competitors in a positive way by announcing its products are not made in Sri Lanka.

Voting against: Shareholders who believe that the company is adequately addressing the issue through its code, compliance and philanthropic programs will vote against the proposal, especially those who believe Gap's programs are having a positive influence on human rights and working conditions in Sri Lanka. Others who believe the decision to leave Sri Lanka is best left to management's discretion or who believe Gap's withdrawal would have little effect on Sri Lanka's human rights record also will vote against this proposal.

Resources

- U.S. Department of State *2010 Human Rights Report: Sri Lanka*
<http://www.state.gov/j/drl/rls/hrrpt/2010/sca/154486.htm>
- Amnesty International report, *Sri Lanka: Briefing to Committee Against Torture*
<http://www.amnesty.org/en/library/asset/ASA37/016/2011/en/2bb1bbe4-8ba5-4f37-82d0-70cbfec5bb2d/asa370162011en.pdf>
- United Nations *Report of the Secretary General's Panel of Experts on Accountability in Sri Lanka:*
http://www.un.org/News/dh/infocus/Sri_Lanka/POE_Report_Full.pdf
- Senate resolution on Sri Lanka from March 1, 2011
<http://thomas.loc.gov/cgi-bin/query/z?c112:S.RES.84>
- Gap's *Code of Vendor Conduct*
http://www.gapinc.com/content/dam/csr/documents/COVC_070909.pdf
- Information on Gap's supplier compliance program
<http://www.gapinc.com/content/csr/html/Goals/supplychain.html>
- Information on the International Labor Organization and International Finance Corporation joint Better Work program
http://www.gapinc.com/content/csr/html/Goals/supplychain/our_program_in_action/ilo_ifc_better_workprogram.html
- Gap 2010 factory ratings by geographic region
http://www.gapinc.com/content/csr/html/Goals/supplychain/data/factory_ratings_by_geographic_region.html
- Gap's human rights policy
http://www.gapinc.com/content/dam/csr/documents/HumanRightsPolicy_FINAL.pdf
- Gap's discussion of Sri Lanka in its sustainability reporting on its website
http://www.gapinc.com/content/csr/html/Goals/supplychain/our_program_in_action/sri_lanka.html
- State department background notes on Sri Lanka's government and economy
<http://www.state.gov/r/pa/ei/bgn/5249.htm#econ>