Congressional-Executive on China

Hearing on: FACTORIES AND FRAUD IN THE PRC: HOW HUMAN RIGHTS VIOLATIONS MAKE RELIABLE AUDITS IMPOSSIBLE

Written testimony by Dr. Alicia Hennig,
Business Ethics Researcher and Interim Professor at Technical University Dresden, Germany

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The Evolution of Forced Labor Research on China

By the end of 2018 at the latest, it became clear that Uyghurs and other members of the Turkic Muslim community in the northwestern Xinjiang Uyghur Autonomous Region (XUAR) were not only being held indefinitely in internment camps without trial, but that these growing camp structures were also linked to forced labor (Buckley & Ramzy 2018). Initial analysis of satellite imagery revealed industrial complexes on the grounds of what the Chinese government calls "re-education" camps (Killing et al. 2020). These first glimpses were associated with the production of textiles, tomatoes, and sugar. In this context, the clothing companies Adidas and C&A were the first German companies to come into the spotlight in 2019 (Dou & Deng 2019). Journalists also began to scrutinize the German car manufacturer Volkswagen due to its subsidiary in Ürümqi together with the company's Chinese joint venture partner SAIC (Brant 2019).

A first comprehensive list of 68 Global Fortune 500 companies from Europe linked to XUAR was compiled by Benjamin Haas/MERICS and published by China File in September 2019. Later that year, leaks (The Xinjiang Papers, China Cables) revealed the brutal and systematic nature of the government's campaign against Uyghurs and other members of the Turkic Muslim community under then-Party Secretary Chen Quanguo (Ramzy & Buckley 2019; Allen-Ebrahimian 2019). In response to these findings and revelations, more and more German companies came under pressure to explain their ties to XUAR (Ankenbrand & Germis 2019).

Investigations into forced labor then took center stage. From 2021, the first detailed reports on forced labor in specific sectors in XUAR were published by Washington DC-based Horizon Advisory on solar (unpublished), on aluminum (2022), and again on solar (2024). Another study on the solar industry was conducted by Bloomberg (2021).

In early 2020, the Australian Strategic Policy Institute (ASPI) published the first comprehensive report on foreign corporate ties to XUAR, analyzing the links between detention camps, factories, and supply chains (Xu et al. 2020). This report identified 82 foreign and Chinese companies that may have directly or indirectly profited from forced labor. A previous publication by Zenz (2019) already revealed that forced labor was not limited to XUAR, but also occurred in other Chinese provinces through a sophisticated state-organized labor transfer program.

From May 2021, this line of research was extended by focusing on Chinese companies from specific sectors in XUAR. A number of such reports were published by researchers at the Helena Kennedy Center at the University of Sheffield UK (SHU). These reports have looked specifically at forced labor in the solar (Murphy & Elimä 2021, Crawford & Murphy 2023), cotton (Murphy et al. 2021), polyvinyl chloride (PVC) or vinyl (Murphy, Valette & Elimä 2022), and automotive (Murphy et al. with NomoGaia 2022) supply chains. The most recent of these studies was published by Human Rights Watch (HRW) on aluminum and the automotive sector in 2024. Over the years, more and more Chinese companies participating in

government programs related to forced or coerced labor have come to light, as well as foreign companies buying from such companies.

With this written testimony I seek to determine the type of ties German companies are having with XUAR and their exposure to state-sponsored forced labor risks associated with their business operations and physical presence in the region.

Methodological Approach
My assessment for this written testimony is based on the available studies mentioned above, media articles, publicly available company information, information provided by non-governmental organizations (NGOs), and academic publications.

For a general overview of German companies in XUAR, I reviewed available company lists and relevant studies to determine which German companies have ties to XUAR and the nature of those ties. I compiled available information into a table (please see Appendix 1) and checked for overlap of company names across studies. The scope of this statement is limited to companies mentioned in more than one report.

To provide a more specific assessment of the risks of forced labor associated with the business operations of German companies with ties to XUAR, I also reviewed the results of the studies included in my assessment for scientific reliability. I reviewed the studies for available methodologies, clear definitional boundaries, and a clear level of information about the Chinese suppliers (please see Appendix 2). In addition, I thoroughly analyzed publicly available company information, such as non-financial reports, group statements and codes of conduct, to assess the companies' approaches to risk management and human rights. Due to space limitations, my assessment is limited to three exemplary cases from the German automotive sector.

The assessment of forced labor risks is complemented by a discussion of the current state of social auditing in China and auditing in China more generally. This discussion is based on recent media articles, recent Chinese legislation and academic publications.

German Companies in XUAR – Overview
The first list by Haas (2019) broadly captured all companies with ties to XUAR and included 68 companies from various industries, 19 of which were German.[1] There were seven companies with supply chain ties to XUAR (Adidas, Bayer, BWM, Daimler, Mercedes-Benz, Metro, and Volkswagen), two with production sites (Volkswagen, BASF), two with offices or locations (Deutsche Bahn, Deutsche Post), three companies that sell equipment (Bosch, Siemens, and ThyssenKrupp), two that primarily provide services or support remotely (Munich Re Group, SAP), and one that builds energy facilities (Linde).
An overlap check with more detailed and recent studies by ASPI, SHU and HRW limited the original sample of 19 companies to eight. In addition, only these studies more specifically linked the companies' relationships to potential forced labor risks associated with their supply chains. The affected German companies are Adidas from the apparel sector; German

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[1] However, a tie does not automatically imply potential risks with regard to complicity in forced labor or otherwise supporting the regime. For example, Lufthansa is holding a minority stake in an Airline catering company in XUAR. Deutsche Bank was lending money to a company in XUAR. As there is no more information provided beyond this, the implications weren't entirely clear.

carmakers BMW, Daimler, Mercedes-Benz and Volkswagen, and Bosch and Siemens from the technology/engineering sector.[2]

The studies reveal potential risks that appear to be concentrated in the following industry sectors: apparel/textiles, automotive, and technology. The corporate activities involved are: potentially sourcing materials from Chinese suppliers linked to forced labor in the case of Adidas, BMW, Daimler, MB, and VW; and selling to or developing technology for Chinese companies implicated in the state-sponsored repression of Uyghurs and other members of the Turkic Muslim community in XUAR. In the case of VW, additional risks arise from the fact that it also has plants in the disputed region via its JV. With a physical presence, a company is more exposed to the risks of forced labor directly at its own plant and on its own property.

Focus on German Automotive Companies

This section looks into three companies: BMW, Mercedes-Benz (MB) and Volkswagen (VW).

Basic Company Information

The three automakers have different positions in the Chinese market. VW's first joint venture (JV) dates back to 1987. Today, VW has JVs with three Chinese companies: SAIC, FAW and JAC, in which VW owns 50 percent, 40 percent and 75 percent, respectively. Its business in China includes 39 plants and employs 90,000 people. In 2023, the company sold 3.2 million cars in China[3] (Annual Report 2023, 35). Sales in China (only including SAIC and FAW) for 2023 are EUR 87,328 million, which is about 27 percent of the group sales of EUR 322,284 million (ibid., 294, 2). Sales are highest in Europe with 40 percent, followed by China with almost 36 percent and the USA with 10 percent (ibid., 120).

While VW can be considered a pioneer, the other two German companies followed much later. MB did not enter China until 2001. The company has a JV with BAIC, which is divided into two locations, Beijing and Fujian. MB owns 49 percent and 50 percent, respectively. The JV includes three plants. In 2023, the company has sold 737,200 units in China (Annual Report 2023, 46). Revenue in China in 2023 is EUR 25,284 million, which is about 16 percent of group revenue of EUR 153,218 million (ibid., 48). Unit sales are highest in China at 36 percent, followed by Europe at 21 percent and the US at 15 percent (ibid., 33).

BMW entered the Chinese market in 2003 and partnered with Brilliance. BMW owns 75 percent of this JV, which includes three plants and employs 26,000 people. In 2023, the company sold 826,257 units (Annual Report 2023, 67). The group turnover is 155,498 million EUR (there is no information about the turnover of BWM Brilliance in China) (ibid., 10). Unit sales are highest in Europe with 37 percent, followed by China with about 32 percent, followed by the USA with about 15 percent (ibid., 67).

Even this basic company information reveals significant differences between these three German automakers. From the number of JVs and plants to the number of cars sold in China and the revenue generated, VW is clearly larger than MB and BMW. However, the Chinese market plays an important role in terms of sales for all companies, accounting for more than 30 percent of their sales. All companies are also dependent on sourcing materials from China but only VW also has a plant in XUAR, which increases its exposure to the risk of forced labor. As early as 2013, when SAIC Volkswagen was about to open its new plant in Xinjiang, journalists described it as the riskiest location in China (Mattheis 2013).

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[2] Chemical giant BASF is not mentioned in any study but frequently in the media and thus also belongs to the German companies exposed to forced labor risks in XUAR/China.

[3] Audi sold another almost 730,000 cars in the premium and sports segment.

German Automotive Companies and their Ties to XUAR

An analysis of information on German automakers with ties to XUAR provided in reports by ASPI (Uyghurs for Sale 2020), SHU (Driving Force 2022), and HRW (Asleep at the Wheel 2024) reveals varying degrees of exposure to state-sponsored forced labor risks associated with their operations -- assuming these suppliers can actually be confirmed by the companies in question.

In these three reports, the following Chinese suppliers from various industries have been identified as being linked to state-sponsored forced labor: EVTech, Highbroad Advanced Material Co., Ltd. (ASPI 2020 report only), Ningbo Joyson Electronics Co., Ltd., Shenzhen Deren Electronics Co., Ltd. for electronic or other technical components; Chalco Ruimin (HWR 2024 report only), Jingwei Group, Minth Group, Shandong Nanshan Aluminum Co. Ltd. for aluminum parts; China Baowu Iron and Steel Group Co. for steel parts; and Camel Group, CATL, China Energy Lithium Co. for batteries.

The mentioned suppliers are said to supply BMW, MB and VW. BMW sources from **five** suppliers: CATL, China Energy Lithium, Jingwei Group, Minth Group and Shenzhen Deren; MB sources from **three** suppliers: CATL, Jingwei Group, and Shenzhen Deren; VW sources from **nine** suppliers: Camel Group, CATL, China Baowu Iron and Steel Group, Chinalco/Chalco, EVTech, Jingwei Group, Minth Group, Shandong Nanshan Aluminum, and Shenzhen Deren Electronics.[4]

German Automotive Companies and Human Rights Abuses in XUAR

In terms of specific allegations of human rights abuses and, more specifically, forced labor, each Chinese supplier's case is different (see Driving Force 2022).

Chinese suppliers Camel Group, China Baowu Iron and Steel Group and Xinjiang Asia-Europe Rare Metal are alleged to have participated in state-sponsored labor transfers within XUAR involving so-called "surplus labor" (CATL may participate in such programs in the future). Shenzhen Deren Electronics and UFLPA-listed Sichuan Mianyang Jingweida have allegedly participated in state-sponsored labor transfers outside XUAR, in the latter case explicitly involving the transfer of "surplus labor". Shenzhen Deren Electronics allegedly installed additional surveillance equipment and security personnel in the course of receiving these labor transfers.

Camel Group, China Baowu Iron and Steel Group, Xinjiang Zhonghe (supplying Chinalco/ Chalco, Jingwei, Minth Group, linked to BMW, MB and VW) and Sichuan Mianyang Jingweida (supplying EVTech, linked to VW) are allegedly involved in "education", "training" and/or "vocational training". In the case of Camel Group, this "pre-job" training was explicitly ideological and military in nature, lasting ten days on a closed campus from which participants were not allowed to leave. In the case of Sichuan Mianyang Jingweida, it was explicitly ideological and disciplinary. Such training programs in XUAR are now known to be coercive and propagandistic in nature. In addition, Xinjiang Zhonghe and China Baowu Iron and Steel Group participated in repressive government programs such as "employment assistance" and surveillance/control measures such as the *fanghuiju* campaign. The specific involvement of Shandong Nanshan Aluminum is difficult to determine.

Taken together, the allegations in these reports range from participation in state-sponsored labor transfers, to involvement in various forms of education – both of which involve coercion – to participation in repressive government programs related to surveillance and control of the Uyghur population and other members of the Turkic Muslim community.

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[4] Camel Group (relevant in the case of VW), Xinjiang Asia-Europe Rare Metal (allegedly supplies China Energy Lithium Co., relevant in the case of BMW) and Sichuan Mianyang Jingweida (allegedly supplies EVTech, relevant in the case of VW) are also listed on the UFLPA entity list (Homeland Security n.d.).

Different types of forced labor
To adequately assess the responsibility and accountability of foreign companies and working measures on the national level it is crucial to clearly differentiate between the two types of forced labor Uyghurs and other members from the Turkic Muslim community are exposed to. In this section, I am drawing on work by Adrian Zenz (2023), as his differentiation has been also included in the UN High-Commissioner's *OHCHR Assessment of human rights concerns* in August 2022.

One type of forced labor is associated with the Vocational Skills Education and Training Centers (VSETCs) and the *laojiao* 劳教 (re-education through labor) system in China more broadly. Here, former prisoners are forced to work in factory parks or elsewhere. It involves low-skilled work in manufacturing, for example, but is not associated with the cotton or polysilicon industries (Zenz 2023, 651). This forced factory work is essentially the final stage of a "gradual release process" after skill training (in the camps) and vocational training (in nearby factories) combined with re-education (ibid., 662). It is often characterized by almost no pay "and work in highly securitized environments" (ibid., 651). As lower security camps began to be closed in 2019, this probably also brought an end to this type of camp-based forced labor (ibid., 651).
The other type of forced labor is linked to the Chinese government's national poverty alleviation programs, specifically the "Poverty Alleviation through Labor Transfer" (转移就业脱贫) policy, which involves the transfer of so-called "rural surplus labor" (ibid., 650). This policy has been in place since 2017, and is linked to annual targets under Xi Jinping's national fight against absolute poverty. Under Xinjiang's 14th Five-Year Plan to Promote Employment (2021-25), this policy requires everyone to be mobilized for work, including students and the elderly. Employment rates must be kept stable, which means enforced retention of workers through surveillance and also indoctrination through "thought education"; state approval is required to leave work (ibid., 660). It was also reported that individuals were threatened with imprisonment if they refused to work under this system. Thus, its implementation is clearly based on coercion. This type of forced labor is associated with low-skilled work in the agricultural sector (harvesting crops), polysilicon production relevant to the renewable energy industry, and the coal industry (ibid., 651; HRW, 2024). These labor transfers are said to have increased since 2021 and "now constitute Xinjiang's primary forced labor system" (ibid.).
In brief, the two systems potentially overlap, as individuals may find themselves in similar work environments, but each system is based on different policies with different objectives and modes of implementation: While forced labor in the context of VSETCs is tied to the Chinese government's goal of "de-extremization" and involves former prisoners, labor transfers or so-called rural surplus labor serves precisely to prevent extremism in the eyes of the Chinese government (ibid., 663).

As I understand the allegations in the above reports, these are rather not related to VSETC forced labor, but to labor transfers. Accordingly, such transfers of surplus labor appear to be the main driver of alleged state-sponsored forced labor at Chinese suppliers.

German Automotive Companies and Measures for Human Rights Protection
All automotive companies in this sample have various measures in place to manage human rights risks in supply chains and to protect human rights. Measures typically include codes of conduct, corporate human rights policies, responsible sourcing guidelines or similar, adherence to voluntary global guidelines, whistleblowing mechanisms and a risk management approach (see Appendix 3 for details on BMW, MB and VW).

The responsibility of companies to protect human rights can be broadly divided into two categories: extra-legal and legal. For decades, this responsibility was only extra-legal and therefore voluntary, a so-called "soft law". Numerous global organizations, such as the OECD, the UN and the ILO, have developed principles, guidelines and other instruments. These are aimed at self-regulation by companies. The companies in this sample all address the prohibition of forced labor in their documents and all adhere to the UN Guiding Principles, among others.

The companies also face reporting requirements under the UK Modern Slavery Act, as well as reporting and due diligence requirements regarding their environmental and social responsibilities under the German Supply Chain Responsibility Act (Lieferkettensorgfalts-pflichtengesetz, LkSG). However, this trend towards the juridification of corporate human rights responsibilities is a more recent phenomenon[5] and, particularly in Germany, the result of ineffective corporate self-regulation.[6]

On Audits in China

A social audit seeks to evaluate a company's performance with regard to its social impact. In this context, measures and procedures in place and their effectiveness are reviewed and assessed. A corporation can use audits and certifications to demonstrate compliance with regulation (HRW 2022).

A report by Human Rights Watch in 2022 already highlighted a number of issues related to such audits, such as the pricing and the time allocated to the audits, which affect quality. When the audit is paid for by the supplier rather than the brand, conflicts of interest are even more pronounced, as suppliers may want to prevent negative findings from reaching the brand. Some consultancies specifically coach suppliers on how to manipulate audit mechanisms. The whole industry is very opaque, as no results are published. Moreover, audits as such can only report findings and make recommendations for improvement. The implementation of these recommendations still depends on the willingness of the supplier and/or the brand. HRW concludes that audits and certifications are "an inadequate tool to ensure respect for human rights and environmental standards" (HRW 2022, 4). Issues such as imposed time constraints, expectations of a favorable outcome, forged certificates, and audit manipulation have also been reported in the case of China (Rocafort 2020, Heras-Saizarbitoria & Boiral 2019, Bermingham & Zhou 2021).[7] A recent report by China Labor Watch again highlights appalling working conditions in China's consumer electronics sector (CLW 2023). In the case of China, all of these issues are also rooted in a general conflict between goals to improve society, such as environmental and social policies, and implementation at the local level, which often conflicts with economic goals (Du & Yi 2022). Furthermore, the prevalence of *guanxi* (social networks) increases conflicts of interest and plays a role in fraudulent audits (He et al. 2017, Bermingham & Zhou 2021). In addition, state-independent media is largely absent, so-called citizen journalists (civilian reporters) and critical citizens are systematically suppressed by the government (Hennig 2024).

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[5] An exception here is the Section 307 of the US Tariff Act (1930). It seems, however, its enforcement has been difficult and it was never applied systematically (Congressional Research Service 2023).

[6] The previous National Action Plan (2016-2020) was based on self-regulation and the voluntary implementation of the UN Guiding Principles. Yet, within four years less than 20 per cent of German companies implemented the UN Guiding Principles. The consequence was a juridification of corporate human rights responsibilities (Bundesministerium für Arbeit und Soziales n.d.).

[7] This also applies to environmental protection. Local government officials are fabricating environmental reports, actively covering up companies' environmentally harming practices (Cyranoski 2019). Legislation that promotes the disclosure of environmental data and preventing greenwashing is not in place yet (CMS Legal Services n.d.).

Aside from general issues, the recent revision of the *Anti-Espionage Law of the People's Republic of China* in April 2023, which took effect in July 2023, has implications for the consulting and auditing industry, as well as other multinational companies operating in China. The revision is said to significantly control and restrict access to data and information, while the definition of espionage is broad and its implications unclear, leaving considerable room for discretionary and arbitrary action (Allen n.d.). Recent crackdowns on auditing firms also do not signal a positive outlook for the industry (Palmer & Zhuang 2023). In light of these developments, independent third-party audits will become increasingly difficult, if not impossible, in China. Regardless, state-sponsored forced labor, and Uyghur forced labor in particular, is already an extremely sensitive issue that companies are unlikely to address in audit conclusions or publicly (HRW 2024). In XUAR, independent audits have been nearly impossible since 2020, as major auditing firms, including Germany's TÜV Süd, have left the region due to pervasive repression (Dohmen 2021).

Concluding Assessment of German Automotive Companies' Measures
Combining the basic company information with the information on their Chinese suppliers provides more context to each company's exposure to forced labor risks in their supply chains. VW, with its three JVs and 39 plants, is linked to nine Chinese suppliers that have been found to be involved in forced labor. VW also has a controversial plant in XUAR. BMW and MB have only one JV and 3 plants each. BMW has five Chinese suppliers, MB only three. VW generates more than three times as much revenue in China as MB and sells more than twice as many cars in the Chinese market as BMW and MB combined. As a result, VW's exposure is much higher than that of its competitors.

All three automakers have implemented a number of more or less similar measures to manage human rights risks in their supply chains. MB has even linked human rights targets to compensation (MB Sustainability Report 2023, 149). All companies state that their supplier/business partner code of conduct applies to all suppliers. They also all conduct n-tier supplier risk assessments, but with nuanced differences (please see Appendix 3 for details). BMW Brilliance audits n-tier suppliers in China based on a third-party audit program.[8] No specific China-related information is available for the other two companies. Given the current political and regulatory environment in China, it remains unclear how many suppliers have been audited and how. In light of this, and the grave situation in XUAR, it is highly questionable to what extent the audit at VW last November, conducted by Löning - Human Rights & Responsible Business/Berlin[9] and lawyers from a firm in Shenzhen, could provide any reliable conclusions.[10]
Thus, the ultimate question regarding companies and human rights risk management is not so much whether companies have a set of measures in place, but rather to what extent these measures still work in the context of an increasingly repressive China, and particularly a pervasively repressive XUAR. Effectiveness also depends on the extent to which these companies themselves are exposed to such risks by virtue of their level of investment and physical presence in China and, more specifically XUAR.

Conclusion
The conclusion of this assessment is that no matter what sophisticated measures and mechanisms companies currently have in place, their effectiveness is severely compromised

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[8] In the 2022 report, only 10 are mentioned, which cannot represent the full range as the supply chains downstream are not included.
[9] Markus Löning conducted the audit himself but he also mentioned the limitations (VW 2023).
[10] In this regard, it also needs to be questioned why MSCI accepted this audit and removed the red flags (Waldersee 2023).

in repressive environments such as China, and XUAR in particular. Moreover, the problem in XUAR goes much deeper than forced labor. Forced labor is only one of several observable features of a policy of repression and destruction that is quietly taking place there. Moreover, the situation will not substantially change until this policy of repression is ended. Under current Party Secretary Ma Xingrui "anti-terrorism" measures and the "Sinicisation of Islam" will continue (People's Government of the Xinjiang Autonomous Region 2024). There is no reason why labor transfers involving surplus labor, which currently seem to be the main driver, would be discontinued in the near future. XUAR is a crucial region for economic growth in China and linked to the Belt-and-Road (BRI) initiative.

Our current set of governmental and corporate tools is only able to capture a part of it, namely all of this deeply entrenched ideology that is operationalized by the Chinese government and therefore visible. Everything else that is less visible, such as repressive government campaigns like *fanghuiju* that have been reported by escaped witnesses, is difficult to capture. But there are ways to expand the toolbox.

Recommendations to the U.S. Government
For businesses, China has become a minefield of rules and regulations. For many multinationals, complying with all these regulations has become overwhelming and they have left or plan to leave. For those who stay, as they are heavily invested in China, such as VW, the risk level will remain, but the current corporate tools are not entirely effective in managing the risks sufficiently.

I have three recommendations (which ideally should be considered by other governments as well)

1) In line with recommendations by HRW (2024, 10), I strongly recommend better mapping of supply chains to increase transparency and knowledge – and these need to be disclosed though not necessarily publicly. However, unlike HRW, I do not believe this should be done through self-regulation. Self-regulation is often a paper tiger: performance is not systematically assessed and there are no sanctions for non-compliance. As a result, to my knowledge, there is not a single voluntary global initiative that could achieve anything close to a level playing field in its respective area. Therefore, supply chain mapping must be made mandatory, especially for high-risk countries for forced labor such as China.
2) In addition to this, I strongly recommend more transparency on audits in designated high-risk countries for forced labor such as China.
3) In light of new legislation at the EU level (the Corporate Sustainability Due Diligence Directive (CS3D) and the introduction of a ban on forced labor), more cooperation is desired in terms of – but not limited to – shared entity lists and implementation of mechanisms (rebuttal of evidence).

This testimony has the following appendices:
- Appendix 1 – German companies with ties to XUAR (https://tinyurl.com/mryzcenx)
- Appendix 2 – Source Reliability Assessment (https://tinyurl.com/wpnz9wcy)
- Appendix 3 – German Automotive Companies and Measures for Human Rights Protection (complete version) and Assessment of German Automotive Companies Measures ((complete version) (https://tinyurl.com/2p7jze68)
- Appendix 4 – References (https://tinyurl.com/57k9wzvt)