

CASE 17

Mattel Responds to Ethical Challenges*

INTRODUCTION

Mattel, Inc. is a global leader in designing and manufacturing toys and family products. Well-known for brands such as Barbie, Fisher-Price, Disney, Hot Wheels, Matchbox, Tyco, Cabbage Patch Kids, and board games, the company boasts nearly \$5.9 billion in annual revenue. Headquartered in El Segundo, California, with offices across the world, Mattel markets its products in over 150 nations.

It all started in a California garage workshop when Ruth and Elliot Handler and Matt Matson founded Mattel in 1945. The company started out making picture frames, but the founders soon recognized the profitability of the toy industry and switched their emphasis to toys. Mattel became a publicly owned company in 1960, with sales exceeding \$100 million by 1965. Over the next forty years, Mattel went on to become the world's largest toy company in terms of revenue.

In spite of its overall success, Mattel has had its share of losses over its history. During the mid to late 1990s, Mattel lost millions to declining sales and bad business acquisitions. In January 1997, Jill Barad took over as Mattel's CEO. Barad's management-style was characterized as strict and her tenure at the helm proved challenging for many employees. While Barad had been successful in building the Barbie brand to \$2 billion by the end of the 20th century, growth slowed in the early 21st. Declining sales at outlets such as Toys "R" Us marked the start of some difficulties for the retailer, responsibilities for which Barad accepted and resigned in 2000.

Robert Eckert replaced Barad as CEO. Aiming to turn things around, Eckert sold unprofitable units and cut hundreds of jobs. In 2000, under Eckert, Mattel was granted the highly sought-after licensing agreement for products related to the *Harry Potter* series of books and movies. The company continued to flourish and build its reputation, even earning the Corporate Responsibility Award from UNICEF in 2003. Mattel released its first Annual Corporate Responsibility Report the following year. In 2011 Mattel was recognized as one of *Fortune* magazine's "100 Best Companies to Work For" for the fourth consecutive year.

MATTEL'S CORE PRODUCTS

Barbie and American Girl

Among its many lines of popular toy products, Mattel is famous for owning top girls' brands. In 1959, Mattel introduced a product that would change its future forever: the Barbie doll. One of the founders, Ruth Handler, had noticed how her daughter loved playing with paper cutout dolls. She decided to create a doll based on an adult rather than on a baby. Barbie took off to become one of Mattel's critical product lines and the number one girls' brand in the world. Since her introduction, Mattel has sold more than 1 billion Barbie dolls in over 150 countries. The Barbie line today includes dolls, accessories, Barbie software, and a broad assortment of licensed products such as books, apparel, food, home furnishings, home electronics, and movies.

To supplement the Barbie line, in 1998 Mattel acquired a popular younger type of doll. Mattel announced it would pay \$700 million to Pleasant Co. for its high-end American Girl collection. American Girl dolls are sold with books about their lives, which take place during important periods of US history. The American Girls brand includes several book series, accessories, clothing for dolls and girls, and a magazine that ranks in the top ten American children's magazines.

Hot Wheels

Hot Wheels roared into the toy world in 1968. More than thirty years later, the brand is hotter than ever and includes high-end collectibles, NASCAR (National Association for Stock Car Auto Racing) and Formula One models for adults, high-performance cars, track sets, and play sets for children of all ages. The brand is connected with racing circuits worldwide. More than 15 million boys aged five to 15 are avid collectors, each owning forty-one cars on average. Two Hot Wheels cars are sold every second of every day. The brand began with cars designed to run on a track and has evolved into a "lifestyle" brand with licensed Hot Wheels shirts, caps, lunch boxes, backpacks, and more. Together, Hot Wheels and Barbie generate 45 percent of Mattel's revenue and 65 percent of its profits.

Cabbage Patch Kids

Since the introduction of mass-produced Cabbage Patch Kids in 1982, more than 90 million dolls have been sold worldwide. In 1994, Mattel took over selling these beloved dolls after purchasing production rights from Hasbro. In 1996, Mattel created a new line of Cabbage Patch doll, called Snacktime Kids, which was expected to meet with immense success. The Snacktime Kids had moving mouths that enabled children to "feed" them plastic snacks. However, the product backfired. The toy had no on/off switch and reports of children getting their fingers or hair caught in the dolls' mouths surfaced during the 1996 holiday season. Mattel voluntarily pulled the dolls from store shelves by January 1997, and offered consumers a cash refund of \$40 on returned dolls. The U.S. Consumer Product Safety Commission applauded Mattel's handling of the Snacktime Kids situation. Mattel effectively managed a situation that could easily have created bad publicity or a crisis situation. Mattel stopped producing Cabbage Patch Kids in 2000.

MATTEL'S COMMITMENT TO ETHICS AND SOCIAL RESPONSIBILITY

Mattel's core products and business environment create many ethical issues. Because the company's products are designed primarily for children, it must be sensitive to social concerns about children's rights. It must also be aware that the international environment often complicates business transactions. Different legal systems and cultural expectations about business can create ethical conflicts. Finally, the use of technology may present ethical dilemmas, especially regarding consumer privacy. Mattel has recognized these potential issues and taken steps to strengthen its commitment to business ethics. The company also purports to take a stand on social responsibility, encouraging its employees and consumers to do the same.

Privacy and Marketing Technology

One issue Mattel has tried to address repeatedly is that of privacy and online technology. Advances in technology have created special marketing issues for Mattel. The company recognizes that, because it markets to children, it must communicate with parents regarding its corporate marketing strategy. Mattel has taken steps to inform both children and adults about its philosophy regarding Internet-based marketing tools, such as the Hot Wheels website. This website contains a lengthy online privacy policy, part of which is excerpted below:

Mattel, Inc. and its family of companies ("Mattel") are committed to protecting your online privacy when visiting a website operated by us. We do not collect and keep any personal information online from you unless you volunteer it and you are 13 or older. We also do not collect and keep personal information online from children under the age of 13 without consent of a parent or legal guardian, except in limited circumstances authorized by law and described in this policy. . . .!

By assuring parents that their children's privacy will be respected, Mattel demonstrates that it takes its responsibility of marketing to children seriously.

Expectations of Mattel's Business Partners

Mattel, Inc. is also making a serious commitment to business ethics in its dealings with other industries. In late 1997, the company completed its first full ethics audit of each of its manufacturing sites as well as the facilities of its primary contractors. The audit revealed that the company was not using any child labor or forced labor, a problem plaguing other overseas manufacturers. However, several contractors were found to be in violation of Mattel's safety and human rights standards and were asked to change their operations or risk losing Mattel's business. The company now conducts an independent monitoring council audit in manufacturing facilities every three years.

In an effort to continue its strong record on human rights and related ethical standards, Mattel instituted a code of conduct entitled Global Manufacturing Principles in 1997. One of these principles requires all Mattel-owned and contracted manufacturing facilities to favor business partners committed to ethical standards comparable with those of Mattel. Other principles relate to safety, wages, and adherence to local laws. Mattel's audits and subsequent code of conduct were designed as preventative, not punitive measures. The company is dedicated to creating and encouraging responsible business practices throughout the world.

Mattel also claims to be committed to its workforce. As one company consultant noted, "Mattel is committed to improving the skill level of workers... [so that they] will experience increased opportunities and productivity." This statement reflects Mattel's concern for relationships between and with employees and business partners. The company's code is a signal to potential partners, customers, and other stakeholders that Mattel has made a commitment to fostering and upholding ethical values.

Legal and Ethical Business Practices

Mattel prefers to partner with businesses similarly committed to high ethical standards. At a minimum, partners must comply with the local and national laws of the countries in which they operate. In addition, all partners must respect the intellectual property of the company, and support Mattel in the protection of assets such as patents, trademarks, or copyrights. They are also responsible for product safety and quality, protecting the environment, customs, evaluation and monitoring, and compliance.

Mattel's business partners must have high standards for product safety and quality, adhering to practices that meet Mattel's safety and quality standards. In recent years, however, safety standards have been seriously violated, which will be discussed in more detail later. Also, because of the global nature of Mattel's business and its history of leadership in this area, the company insists that business partners strictly adhere to local and international customs laws. Partners must also comply with all import and export regulations. To assist in compliance with standards, Mattel insists that all manufacturing facilities provide the following:

- Full access for on-site inspections by Mattel or parties designated by Mattel
- Full access to those records that will enable Mattel to determine compliance with its principles
- An annual statement of compliance with Mattel's Global Manufacturing Principles, signed by an officer of the manufacturer or manufacturing facility²

With the creation of the Mattel Independent Monitoring Council (MIMCO), Mattel became the first global consumer products company to apply such a system to facilities and core contractors worldwide. The company seeks to maintain an independent monitoring system that provides checks and balances to help ensure that standards are met.

If certain aspects of Mattel's manufacturing Principles are not being met, Mattel will try to work with them to help them fix their problems. New partners will not be hired unless they meet Mattel's standards. If corrective action is advised but not taken, Mattel will terminate its relationship with the partner in question. Overall, Mattel is committed to

both business success and ethical standards, and it recognizes that it is part of a continuous improvement process.

Mattel Children's Foundation

Mattel takes its social responsibilities very seriously. Through the Mattel Children's Foundation, established in 1978, the company promotes philanthropy and community involvement among its employees and makes charitable investments to better the lives of children in need. Funding priorities have included building a new Mattel Children's Hospital at the University of California, Los Angeles (UCLA), sustaining the Mattel Family Learning Program, and promoting giving among Mattel employees.

In November 1998, Mattel donated a multiyear, \$25 million gift to the UCLA Children's Hospital. The gift was meant to support the existing hospital and provide for a new state-of-the-art facility. In honor of Mattel's donation, the hospital was renamed Mattel Children's Hospital at UCLA.

The Mattel Family Learning Program utilizes computer learning labs as a way to advance children's basic skills. Now numbering more than eighty throughout the United States, Hong Kong, Canada, and Mexico, the labs offer software and technology designed to help children with special needs or limited English proficiency.

Mattel employees are also encouraged to participate in a wide range of volunteer activities as part of "Mattel Volunteers: Happy to Help." Employees serving on boards of local nonprofit organizations or helping with ongoing nonprofit programs are eligible to apply for volunteer grants supporting their organizations. Mattel employees contributing to higher education or to nonprofit organizations serving children in need are eligible to have their personal donations matched dollar for dollar up to \$5,000 annually.

International Manufacturing Principles

As a U.S.-based multinational company owning and operating facilities and contracting worldwide, Mattel's Global Manufacturing Principles reflect not only its need to conduct manufacturing responsibly, but to respect the cultural, ethical, and philosophical differences of the countries in which it operates. These Principles set uniform standards across Mattel manufacturers and attempt to benefit both employees and consumers.

Mattel's Principles cover issues such as wages, work hours, child labor, forced labor, discrimination, freedom of association, and working conditions. Workers must be paid at least minimum wage or a wage that meets local industry standards (whichever is greater). No one under the age of 16 or the local age limit (whichever is higher) may be allowed to work for Mattel facilities. Mattel refuses to work with facilities that use forced or prison labor, or to use these types of labor itself. Additionally, Mattel does not tolerate discrimination. The company states that an individual should be hired and employed based on his or her ability—not on individual characteristics or beliefs. Mattel recognizes all employees' rights to choose to associate with organizations or associations without interference. Regarding working conditions, all Mattel facilities and its business partners must provide safe working environments for their employees.

OVERSEAS MANUFACTURING

Despite Mattel's best efforts, not all overseas manufacturers have faithfully adhered to its high standards. Mattel has come under scrutiny over its sale of unsafe products. In September 2007, Mattel announced recalls of toys containing lead paint. The problem surfaced when a European retailer discovered lead paint on a toy. An estimated 10 million individual toys produced in China were affected. Mattel quickly stopped production at Lee Der, the company officially producing the recalled toys, after it was discovered that Lee Der had purchased lead-tainted paint to be used on the toys. Mattel blamed the fiasco on the manufacturers' desire to save money in the face of increasing prices. "In the last three or five years, you've seen labor prices more than double, raw material prices double or triple," CEO Eckert said in an interview, "and I think that there's a lot of pressure on guys that are working at the margin to try to save money."

The situation began when Early Light Industrial Co., a subcontractor for Mattel owned by Hong Kong toy tycoon Choi Chee Ming, subcontracted the painting of parts of *Cars* toys to another China-based vendor. The vendor, named Hong Li Da, decided to source paint from a non-authorized third-party supplier—a violation of Mattel's requirement to use paint supplied directly by Early Light. The products were found to contain "impermissible levels of lead."

On August 2, 2007, it was announced that another of Early Light's subcontractors, Lee Der Industrial Co., used the same lead paint found on *Cars* products. China immediately suspended the company's export license. Afterward, Mattel pinpointed three paint suppliers working for Lee Der—Dongxin, Zhongxin, and Mingdai. This paint was used by Lee Der to produce Mattel's line of Fisher-Price products. It is said that Lee Der purchased the paint from Mingdai due to an intimate friendship between the two company's owners. On August 11, 2007, Zhang Shuhong, operator of Lee Der, hung himself after paying his 5,000 staff members.

Later that month, Mattel was forced to recall several more toys because of powerful magnets in the toys that could come loose and pose a choking hazard for young children. If more than one magnet is swallowed, the magnets can attract each other inside the child's stomach, causing potentially fatal complications. Over 21 million Mattel toys were recalled in all, and parents filed several lawsuits claiming that these Mattel products harmed their children.

At first, Mattel blamed Chinese subcontractors for the huge toys recalls, but the company later accepted a portion of the blame for its troubles, while maintaining that Chinese manufacturers were largely at fault. The Chinese view the situation quite differently. As reported by the state-run Xinhua news agency, the spokesman for China's General Administration of Quality Supervision and Inspection and Quarantine said, "Mattel should improve its product design and supervision over product quality. Chinese original equipment manufacturers were doing the job just as importers requested, and the toys conformed to the U.S. regulations and standards at the time of the production." Mattel also faced criticism from many of its consumers, who believed Mattel was denying culpability by placing much of the blame on China. Mattel was later awarded the 2007 "Bad Product" Award by Consumers International.

How did this crisis occur under the watch of a company praised for its ethics and high safety standards? Although Mattel had investigated its contractors, it did not audit the entire supply chain, including subcontractors. These oversights left room for these violations to occur. Mattel has also moved to enforce a rule that subcontractors cannot hire suppliers two or three tiers down. In a statement, Mattel says it has spent more than 50,000 hours

investigating its vendors and testing its toys. Mattel also announced a three-point plan. This plan aims to tighten Mattel's control of production, discover and prevent the unauthorized use of subcontractors, and test the products itself rather than depending on contractors.

THE CHINESE GOVERNMENT'S REACTION

Chinese officials eventually did admit the government's failure to properly protect the public. The Chinese government promised to tighten supervision of exported products, but effective supervision is challenging in such a large country that is so burdened with corruption. In January 2008, the Chinese government launched a four-month-long nationwide product quality campaign, offering intensive training courses to domestic toy manufacturers to help them brush up on their knowledge of international product standards and safety awareness. As a result of the crackdown, the State Administration for Quality Supervision and Inspection and Quarantine (AQSIQ) announced that it had revoked the licenses of more than 600 Chinese toy makers. As of 2008, the State Administration for Commerce and Industry (SACI) released a report claiming that 87.5 percent of China's newly manufactured toys met quality requirements. While this represents an improvement, the temptation to cut corners remains strong in a country that uses price, not quality, as its main competitive advantage. Where there is demand, there will be people trying to turn a quick profit.

MATTEL VERSUS FORMER EMPLOYEE AND MGA

In 2004, Mattel became embroiled in a bitter intellectual property rights battle with former employee Carter Bryant and MGA Entertainment Inc. over rights to MGA's popular Bratz dolls. Carter Bryant, an on-again/off-again Mattel employee, designed the Bratz dolls and pitched them to MGA. A few months after the pitch, Bryant left Mattel to work at MGA, which began producing Bratz in 2001. In 2002, Mattel launched an investigation into whether Bryant had designed the Bratz dolls while employed with Mattel. After two years of investigation, Mattel sued Bryant. A year later MGA fired off a suit of its own, claiming that Mattel was creating Barbies with looks similar to those of Bratz in an effort to eliminate the competition. Mattel answered by expanding its own suit to include MGA and its CEO, Isaac Larian.

For decades, Barbie has reigned supreme on the doll market. However, Bratz dolls have given Barbie a run for her money. In 2005, four years after the brand's debut, Bratz sales were at \$2 billion. At the same time, Barbie was suffering from declining sales. In 2008 Barbie's gross sales fell by 6 percent. Many analysts believe that Barbie has reached the maturity stage of its product life cycle.

Four years after the initial suit was filed, Bryant settled with Mattel under an undisclosed set of terms. In July 2008, a jury deemed MGA and its CEO liable for what it termed "intentional interference" regarding Bryant's contract with Mattel. In August 2008, Mattel received damages in the range of \$100 million. Although Mattel first requested damages of \$1.8 billion, the company is pleased with the principle behind the victory.

In December 2008, Mattel appeared to win another victory when a California judge banned MGA from issuing or selling any more Bratz dolls. However, the tide soon turned on Mattel's victory. In July 2010, the Ninth U.S. Circuit Court of Appeals threw out the

ruling. Eventually, the case came down to whether Mattel owned Bryant's ideas under the contract he had with the company. In April 2011, a California federal jury rejected Mattel's claims to ownership. In another blow to Mattel, the jury also ruled that the company had stolen trade secrets from MGA. According to the allegations, Mattel employees used fake business cards to get into MGA showrooms during toy fairs. Mattel was ordered to pay \$85 million in liabilities, plus an additional \$225 million in damages and legal fees. MGA CEO Isaac Larian has also announced that he will file an antitrust case against Mattel. Mattel continues to claim that Bryant violated his contract when he was working for the company.

MATTEL LOOKS TOWARD THE FUTURE

Like all major companies, Mattel has weathered its share of storms. The company has faced a series of difficult and potentially crippling challenges, including the recent verdict against the company in the Bratz lawsuit. During the wave of toy recalls, some analysts suggested that the company's reputation was battered beyond repair. Mattel, however, has refused to go quietly. Although the company admits to poorly handling recent affairs, it is attempting to rectify its mistakes and to prevent future mistakes as well. With the economic future of the United States uncertain, Mattel may be in for slow growth for some time to come. Mattel is hard at work restoring goodwill and faith in its brands, even as it continues to be plagued with residual distrust over the lead paint scandal and its alleged theft of trade secrets. Reputations are hard won and easily lost, but Mattel appears to be steadfast in its commitment to restoring its reputation.

QUESTIONS

1. Do manufacturers of products for children have special obligations to consumers and society? If so, what are these responsibilities?
2. How effective has Mattel been at encouraging ethical and legal conduct by its manufacturers? What changes and additions would you make to the company's Global Manufacturing Principles?
3. To what extent is Mattel responsible for issues related to its production of toys in China? How might Mattel have avoided these issues?