

# Codes of Responsible Business Conduct When Good Intentions Become Binding

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Voluntary codes of conduct have become common (and even expected) practice as part of a broader corporate social responsibility (CSR) strategy for companies across all industries. Increasingly, companies have been facing litigation and reputational risks in connection with the implementation of their CSR goals and policies as articulated in their codes of conduct.

This article looks at case law where the legal enforceability of CSR codes is at issue and provides practical considerations for their drafting, revision and implementation to minimize legal and reputational risks.

## CODES OF RESPONSIBLE BUSINESS CONDUCT EXPLAINED

Codes of conduct seek to clarify a company's mission, values and principles by developing standards of conduct intended to govern decision-making and business operations, primarily with respect to environmental, social and governance (ESG) issues including human rights, environmental impacts, diversity, transparency and anti-corruption. They are often supplemented by supplier codes of conduct that seek to extend compliance with standards of responsible business conduct throughout a company's supply chain.

In certain cases, codes incorporate international norms such as the United Nations Global Compact's 10 principles, Organisation for Economic Co-operation and Development Guidelines on Multinational Enterprises or International Labour Organization's Fundamental Conventions regarding labour standards and rights of workers.



Most companies publish CSR codes to inform their stakeholders and consumers of their corporate values and how the company seeks to positively contribute to society.

While the lack of adopting or complying with a CSR code (or the alleged non-compliance) can raise significant reputational risks, companies are also increasingly facing litigation risks. There have been a number of cases brought against companies abroad and in Canada, in which the non-binding or voluntary nature of CSR codes of conduct has been challenged.

At this stage, large multinational corporations appear to be the main targets of such legal challenges, often with the goal of raising public awareness to social and environmental issues around the world. That being stated, all companies, large and small, which have either adopted such codes of conduct or undertake to comply with supplier codes of conduct should seriously consider following legal developments in this area.

## LITIGATION RISKS

### Duty to Disclose and Misrepresentation Cases



Over the past several years in the United States, there have been several attempted class action lawsuits taking on major food and confectionery companies for not disclosing alleged child labour or human trafficking in their supply chains, notably

with respect to the production of cocoa in parts of Africa.

Similar cases have targeted companies providing U.S. consumers with seafood and pet food sourced in Southeast Asia, where claims have been made relating to working conditions on fishing boats or in prawn harvesting operations.

In one case, *Tomasella v. Nestlé USA, Inc.*, which is currently pending before the United States District Court for the District of Massachusetts, a group of consumers is alleging that Nestlé violated the *Massachusetts Consumer Protection Act* by not informing consumers on the sourcing of their chocolate from areas known as using forced labour. To support their claim, the plaintiffs argued that Nestlé's corporate business principles and supplier code specifically prohibit child and slave labour.

Similar arguments have been made in a class action brought against Hershey Co.

To date, courts have dismissed many of these cases because the plaintiff consumers lacked standing or the defendants were found to not have a duty to disclose the alleged human rights abuses in their supply chain because this matter does not have a bearing on the health or safety of the consumers or does not relate to the central function of the product. The former is a test for finding a positive duty to disclose, such as in the case of health warnings required on cigarette packages.

Absent legislation specifically requiring companies to make certain disclosure, such as the *California Transparency in Supply Chains Act* (Supply Chains Act), it is currently difficult in the U.S. to argue that a company has a positive duty to disclose irresponsible or illegal practices in its supply chain or that such non-disclosure constitutes a fraudulent omission. A case based on an affirmative misrepresentation is, arguably, an easier task. This would also be the case in Canada.

While consumers have attempted to rely on breaches under the Supply Chains Act as a basis for alleging contravention of consumer protection legislation, to date, these attempts have been unsuccessful due, notably, to the fact that the Supply Chains Act does not include a direct right of action to consumers. The only available remedy for its contravention is limited to an action by the California Attorney General by way of injunction.

Other jurisdictions, such as the United Kingdom, have adopted legislation (the U.K. *Modern Slavery Act, 2015*) requiring businesses to make certain disclosure.

In many jurisdictions, false, misleading or deceptive representations are considered an unfair or illegal practice under consumer protection legislation.

Depending on the facts in the case and the jurisdiction, an argument based on false representation could be made where a plaintiff consumer can point to a statement set out in a corporate code, which has been found to be untrue or misleading and which the consumer can demonstrate was relied upon when purchasing a product.

However, misrepresentation or false representation must first be established. In 2015, another case against Nestlé involving canned cat food products that were alleged to contain seafood sourced from forced labour was dismissed on several grounds, including because Nestlé had no duty to disclose information and also it was determined that the aspirational wording of Nestlé's code did not constitute misrepresentation. The court found that no reasonable consumer could infer from Nestlé's code that all its suppliers would strictly comply therewith.

These cases illustrate the importance of carefully drafting CSR codes and policies, and of determining which provisions are to be prescriptive and which should be more aspirational.

### Duty of Care and Tort Cases



In 2013, the Ontario Superior Court of Justice (Court) recognized that voluntary codes of conduct and public representations could be used as evidence in establishing a duty of care, in *Choc v. Hudbay Minerals*

*Inc.* In this case, an Indigenous group from Guatemala brought proceedings against a Canadian mining company, Hudbay Minerals Inc. (Hudbay), and its wholly controlled subsidiaries. They alleged that security personnel working for Hudbay's subsidiaries committed human rights abuses while under the control and supervision of the parent company. The central question to the negligence claim in this case was whether Hudbay owed a duty of care to the plaintiffs.

In order to establish a novel duty of care in this case, it must be proven that:

1. The alleged harm is a reasonably foreseeable consequence of the purported breach;
2. There is sufficient proximity between the parties so that it would not be unjust or unfair to impose a duty of care on the defendants (based on factors such as expectations, representations and reliance); and
3. There is no policy-related reason to negate or otherwise restrict that duty.

Hudbay, as part of its human rights policy, had adopted the *Voluntary Principles on Security and Human Rights*, which are human rights guidelines designed for the extractive sector.

The Court has yet to render a ruling on the merits. However, at the preliminary stage, the Court refused to strike out the claims on the basis that Hudbay's public statements concerning its relationship with the local community, its commitment to respecting human rights and its adherence to the *Voluntary Principles on Security and Human Rights* were indicative of a relationship of proximity that is necessary in establishing a *prima facie* duty of care.

Following the collapse of the Rana Plaza factory in Bangladesh in 2013, a class action was brought in Ontario against George Weston Limited (Loblaws), in which the question was raised as to whether a corporation could be liable in tort for non-compliance with a voluntary CSR code. In *Das v. George Weston Limited*, the plaintiff argued that Loblaws had adopted CSR standards providing that it would not purchase goods from suppliers who do not comply with appropriate workplace safety standards. As a result, the plaintiffs alleged that Loblaws had a fiduciary duty to ensure that the interest, health and physical safety of the suppliers' employees were protected.

The court concluded that there existed no fiduciary relationship between Loblaws and the putative class members, but did not exclude the possibility of a fiduciary duty ever originating from a voluntary CSR code.

If the source of the fiduciary duties is the CSR standards, then the language in the CSR standards should clearly support a fiduciary *obligation*, the court stated in obiter, but did not provide any further indication as to what language in a code could ever create sufficient proximity nexus.

This case again illustrates the importance of appropriately crafting the representations included in a CSR code. For more information on this case, see our July 2017 *Blakes Bulletin: Who Is My Neighbour? Ontario Court Rejects a Duty of Care to Employees of Foreign Suppliers*.

## PRACTICAL CONSIDERATIONS



Creative lawsuits seeking to dissolve the boundaries between voluntary initiatives and legal obligations are on the rise. Consequently, a code setting out a company's policies and practices for responsible business conduct should be carefully drafted and regularly revised and updated.

The following is a non-exhaustive summary checklist of practical considerations to take into account when preparing a CSR code for the first time or when conducting a review of an existing corporate code of conduct or CSR policy.

### Due Diligence

A company may choose to develop its own CSR code or adhere to an already developed code that is appropriate for its specific industry. Several industry associations have developed principles that members must adhere to, or have provided model codes that companies may adopt or adapt to their specific needs and ambitions.

Before adopting, developing or revising of a code, it is important to carry out due diligence, including the following:

- ☑ Identify specific issues and risks facing the company and its supply chain, as well as its legal obligations (including ESG reporting).
- ☑ Review the track record of the company (and its suppliers) in the various areas that will be addressed to identify achievements, best practices and potential risks.
- ☑ Verify whether the company already adheres to a set of principles or industry guidelines to determine whether a specific code is needed, or to ensure consistency.
- ☑ Identify short, mid and long-term objectives.

### Drafting

Recent case law shows that the framing of norms in a CSR code is relevant to the issue of enforcement as well as credibility. When drafting a code to promote responsible corporate behaviour while reducing reputational and legal risks:

- ☑ Consider the choice of words and tone used in a CSR code – this is critical for risk management.
- ☑ Adopt clear and simple language and incorporate both aspirational and prescriptive wording where appropriate (i.e., use of “may”, “should” and “strive”; as opposed to “must” and “shall”).
- ☑ Consider factors such as the size of a company, ability to influence outcomes, industry area, geographical scope, etc., when determining the terminology used in a code to identify which goals are realistic to achieve immediately and which are longer term goals.

It is worth noting that if the language used in a code of conduct is too vague and aspirational, it will be difficult for the company adopting the code to implement it, however, it may reduce the risk of creating legal obligations. On the other hand, vague and non-committal language could also give rise to issues of credibility and reputation.

Additionally, some companies use disclaimers in their codes. Disclaimers can serve multiple objectives, such as confirming that the code is not a comprehensive document covering all conduct that is mandated or expected by its suppliers, or confirming that the standards are not guarantees and do not create legal commitments.

As more legal challenges arise, disclaimers may become more prevalent in codes of conduct. The issue then could become determining whether these disclaimers could affect a company's reputation and drafting disclaimers to strike a good balance between addressing reputational and legal risks.

## Capacity and Training

Those tasked with the development or updating of a code should also be mindful of the capacity and tools available to implement and monitor behaviour and practices to avoid risks, both legal and reputational, associated with overpromising and under-delivering.

Once a code has been adopted:

- ☑ Regularly educate and inform employees, officers and contractors (as the case may be) of the existence, interpretation or revision of a code.
- ☑ Verify on a regular basis that such codes are understood and adapted and that training is up-to-date.

## Monitoring and Enforcement

The approach to monitoring varies among companies and industries. Enforcement can present complex issues. In certain cases, a company will adopt measures such as termination of employment or a contract and in other cases, financial penalties will be imposed.

The range of potential consequences may be set out in a CSR code or in the corporate policies. Where risks of non-compliance are identified, a company may seek a more proactive approach to maintain employment or a contractual relationship with a supplier, while assisting the individual or subcontractor to effectively address issues and improve practices (i.e., to improve behaviour, environmental standards or working conditions).

- ☑ Based on a risk assessment analysis, consider whether your company will monitor its officers, employees and/or activities and whether the code's implementation will extend to the supply chain (and to what extent) or rely on its direct contractors to monitor further along the chain.

- ☑ Carefully draft supply, service and employment contracts to address monitoring, third-party audits, enforcement and consequences of non-compliance where appropriate.
- ☑ Determine whether monitoring will be conducted internally or by external auditors.

## CONCLUSION

While the success of recent lawsuits challenging specific representations made by corporations in their CSR codes has been limited to date, these actions have shed light on the importance of drafting and reviewing these documents with care. Some of these lawsuits have been settled for significant amounts and, whether granted, dismissed or settled, such lawsuits could result in tarnishing the corporate image of targeted companies.

Environmental and social responsibility is increasingly considered as being a business imperative. When drafting and revising codes and policies that address ESG matters, it is important to be mindful of both a corporation's reputational and legal risks, as compliance with such values and commitments are increasingly being brought under the spotlight in both the court of public opinion and the legal courts.

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