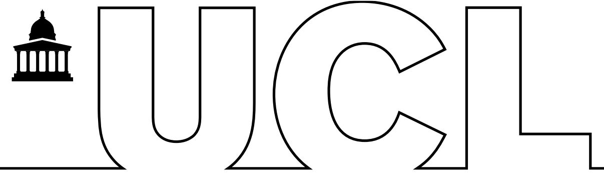

February 25, 2019

Dear Sir or Madam,

Re: *Open-ended intergovernmental working group on transnational-corporations and other business enterprises with respect to human rights: Call for comments and proposals on the draft legally binding instrument*

We wish to make some comments on Article 10, *Legal Liability*, of the draft legally binding instrument. First, we express some concerns that Article 10 seems to fail to take into account the elements outlined in Article 9, *Prevention*, of the instrument. By failing to take into account business' measures of prevention in determining their legal liability, we are concerned that this may lead businesses to take inadequate care in *ex ante* preventing human rights abuses. Second, we believe that the concepts in Article 10(6) for attributing liability to a person/business for misconduct by others lack clarity. Accordingly, we make some suggestions for improvements.

Linking Article 9 and Article 10; Nature of liability

Article 10(6) (concerning civil liability) notes that natural or legal persons with transnational business activities shall be held liable for human rights harms caused in the context of their business activities. While this provision refers to the 'foreseeability' of human rights violations as a factor that can lead to liability (Article 10(6)(c)), it does not make any explicit reference to the prevention measures, required under Article 9 of the instrument. Instead, it holds that a business will be liable if it exercises control over the operations, exhibits a sufficiently close relation with a subsidiary/entity and there is a strong and direct connection between conduct and wrong suffered, or the risk was foreseeable.

This suggests that Article 10(6) is establishing forms of strict liability for businesses, both in the shape of strict direct liability (for harms stemming from a person's own operations) and strict vicarious liability (establishing a person's liability for other's misconduct).[1] That is, once a human rights violation is established, businesses will be liable unless they can demonstrate that they did not exercise control or have a close relation that has a direct connection to harm, or the violation was not foreseeable.

We believe that strict liability is appropriate when it comes to conduct by others (see below on parent/group liability) but that it is not necessarily the best option when it comes to direct liability for a business's own conduct. The problem with quasi-strict liability is that it has a tendency to fail to incentivize rational actors to invest in additional safety or preventative measures.[2] If a business will be held liable for a human rights violation, despite taking all the preventative measures outlined in Article 9, it may be disinclined to adopt due diligence

[1] These include strict vicarious liability (elements a. and b.) and quasi-strict liability (element c.).
[2] See the discussion in B. Choudhury and M. Petrin, *Corporate Duties to the Public* (Cambridge University Press, 2019), pp. 158-159 and the citations therein.

measures or to keep them at a minimum or it could adopt the prevention measures in a box-ticking manner without embracing the spirit of the measures. As the literature on non-financial reporting requirements for businesses has shown, when businesses fail to embrace the spirit of their legal obligations, business behaviour does not fundamentally change.[3] If the purpose of Article 9 is to reorient the business mind set in relation to preventing human rights harms, the remainder of the instrument should work to reinforce this goal and create incentives for businesses to implement effective prevention and monitoring measures.

Articles 10(6); Clarifying direct liability and liability for others

A second problem with Article 10(6) is that although it recognizes the problem of human rights violations occurring in groups of companies and/or within connected companies (including but not limited to supply chains), it does not go far enough in attributing liability in such instances. Furthermore, Article 10(6) introduces various terms and concepts that are not clearly defined.

Article 10(6) seeks to impose liability on a business not only for harm stemming from its own operations/business but also for the acts of other businesses or entities.[4] However, important terms that it uses in doing so, namely “control,” “sufficiently close relation,” “operations,” and “chain of economic activity,” are not defined. It is also not clear what type of conduct would be required in order to establish the necessary “strong and direct connection” between a person’s conduct and human rights harms. Finally, given the current wording it is also not clear what exactly the difference is between liability under elements b. and c. This leaves the conditions of liability under all elements contained in Article 10(6) open to myriad interpretations, leading to legal uncertainty and potential gaps in redress for victims of human rights violations. We are thus concerned that while the proposed system of liability pursues the correct underlying goals, in its current form it might be too unclear to work properly.

We have suggested in previous work a two-pronged group liability system under which parent companies and entire groups of companies would be liable for torts, including human rights violations, stemming from activities of another member/entity of the group.[5] Under the *first prong*, we proposed that there should be liability on corporate groups as a whole for torts by any entity that forms part of the group. While there would still be the requirement that the group member in question needs to meet all the requirements of a specific tort, which could be negligence based (which is the usual case) or strict liability based, once liability is established it would extend to the parent company and group as a whole independent of their own conduct or fault. Under the *second prong*, we proposed a modified system of vicarious liability that seeks to impose liability on parent companies and groups for torts at entities that are not a core part of the group but which are still integrated into a group’s business (i.e. more loosely connected ‘network companies’).

Based on this model, we recommend that Article 10(6) be divided into a provision on a business’s own/direct liability and business liability for human rights violations by other

[3] Ibid. p. 87.
[4] Zero Draft Legally Binding Instrument, art. 10(6)(a) and (b).
[5] Choudhury and Petrin, *supra note* 2, at chapter 5. See also M. Petrin and B. Choudhury, ‘Group Company Liability’ (2018) 19:4 *European Business Organization Law Review* 771.

businesses and entities. In the provision relating to a business' own liability for human rights violation, we suggest including an option for the business being able to rely on a due diligence defence if it has taken sufficient due diligence or preventative measures. Not only would this incorporate the measures outlined in Article 9 but it would also strengthen the general spirit of the provision in Article 10(6)(c).

Next, there should be a section addressing a business's liability for human rights violations by other businesses/entities. The main idea here is to introduce a system that operates with a system of strict liability for parent companies/groups once it is established that a business/entity that is part of the group engaged in a human rights violation, without being able to demonstrate sufficient prevention measures (ie no reliance on a due diligence defence). We thus recommend the following changes to Article 10(6)(a) and (b).

First, instead of determining liability by the extent to which a business 'exercises control over the operations,' (Article 10(6)(a)) we recommend that the existence of a 'group' be determined as a factual matter, and once this is established, that liability be imposed for any human rights violation. One approach to determining the existence of a group is to stipulate that a business will be liable for the human rights violations of another company if the business holds a majority of voting rights, the right to control the majority of the board composition or the majority voting rights in the other company, or the other company is a subsidiary of a company that itself is a subsidiary of the business.[6] An alternative approach is to define a group based on the presence of controlling equity stakes between parent and subsidiary companies, with the size or threshold for finding a 'controlling' stake being defined by a fixed percentage.

Second, we recommend better defining the concept of "close relation" in Article 10(6)(b) to ensure it captures instances where businesses do not have a formal group structure (as defined above) but their businesses are nonetheless integrated. This refers to the second prong of our group liability model. Thus, close relation could be defined where a business: furthers the economic goals or business of the entity whose liability is in question (the "parent entity"); is functionally part of the parent entity's business or part of the business of the group to which the parent entity belongs; or serves the purpose of externalizing liability. These, or comparable elucidations of the concept of "close relation" will help clarify the situations in Article 10(6)(b). As a general guide, the definition of a close relation between businesses should refer to the degree of economic, organisational, and legal links between two or more entities/businesses.

We hope you find this submission useful. If you require any further information, please do not hesitate to contact us.

Yours truly,

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[6] This corresponds to the definition of a subsidiary under the UK's Company Act. Section 1159(1), Company Act, 2006 (UK).