Officer and Director Liability in Transnational Human Rights Litigation

By:

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Tort actions have emerged as a legal strategy for promoting accountability for human rights violations committed by transnational corporations (TNCs) involved in natural resource extraction. In the typical scenario, a parent company incorporated under the laws of a developed state invests in a project in a developing state through a series of subsidiaries. The corporate chain ends with an operating entity established under the developing state's laws, which are lax with respect to labour and environmental standards. In addition, these projects often encounter opposition from the people affected.

The combination of strong financial incentives for both the parent company and developing state, an angry and vulnerable local population, and laws that are often inadequate to protect them has proven to be a recipe for human rights violations. The quest for corporate accountability for such violations reflects the

Goal 10.2 of the UN Sustainable Development Goals, which is to reduce inequality by promoting social, economic, and political inclusion.

Given the challenge posed by complex corporate structures and multiple jurisdictions, one of the first questions that victims' counsel needs to confront is who to sue. In Canada, the predominant strategy is to sue the parent company based on the theory that it is directly responsible for the wrongdoing associated with its operating subsidiary. For example, *in Choc v. Hudbay Minerals Inc*., 2013 ONSC 1414, the plaintiffs alleged that a Canadian mining company was negligent in supervising the activities of its foreign subsidiaries, which employed security forces that committed a series of human rights violations. Despite the fact that the plaintiffs' pleadings alleged wrongdoing by executives of the parent company, the action names only the corporate entities as opposed to the people who directed them: see *Choc* at para. 60. The same is true of a more recent case against a Canadian mining company that operated a project in Eritrea: *Araya v. Nevsun Resources Ltd*., 2017 BCCA 401 at para. 4.

The central argument of this blog post is that suing the agents of the parent company (e.g. its directors or officers) is likely to be a more effective deterrent than suing the parent company itself. In other words, I suggest that personal liability, as opposed to corporate liability, may be a better way of using tort law to ensure that TNCs respect human rights.

The Deterrent Effect of Personal Liability

The main argument in favour of personal liability is that it places the burden directly on the people who are responsible for corporate decisions and policies. Conversely, corporate liability is indirect. It rests on the assumption that since shareholders will ultimately bear the costs of a judgment, they will have a financial incentive to pressure the company to behave responsibly. But there are a number of problems with this assumption.

First, the path to reform is indirect and thus uncertain because the will of shareholders must be translated through multiple levels of the corporate hierarchy. Conversely, personal liability in tort has the potential to affect everyone in this hierarchy. Second, due to coordination problems, it will be

difficult for shareholders to act collectively, especially in the context widely held companies, which are common in extractive industries. Third, because of limited liability, each shareholder only bears a fraction of the risk of corporate wrongdoing, which may be offset by the benefits that accrued prior to its discovery. Fourth, since large TNCs are highly diversified, shareholder losses due to human rights abuses at one site may be offset by profits generated elsewhere. In addition, shareholders, particularly institutional ones, are themselves diversified, meaning the losses associated with one project of one company amid a large portfolio of investments is unlikely to incite much activism.

Finally, shareholders, as non-participants in the wrongdoing, are unlikely to feel stigma as intensely as those who actually carried it out. Even in the most extreme case imaginable, shareholders can liberate themselves of stigma by simply divesting, and the fictional corporate entity can dissolve. But the human beings who were at fault will have a much harder time overcoming the emotional and reputational consequences of what they did. The impact of this personal stigma is something that cannot be indemnified or insured against.

The Legal Basis for Personal Liability

Even if personal liability is desirable from the standpoint of deterrence, it must be a viable legal option. The liability of corporate agents in tort is a subject that’s fraught with misunderstanding, due largely to the interaction between corporate personality and basic principles of tortious liability.

The Ontario Court of Appeal stated the basic principle as follows: “The consistent line of authority in Canada holds simply that, in all events, officers, directors and employees of corporations are responsible for their tortious conduct even though that conduct was directed in a *bona fide* manner to the best interests of the company”: *ADGA Systems v. Valcom* (1999) 43 O.R. (3d) 101. This principle is reflected in the Supreme Court’s earlier judgment in *London Drugs v. Kuehne & Nagel International*, [1992] 3 S.C.R. 299 at 408, which held that employees are not immune from tort liability simply because the wrongdoing occurred in course of their duties.

More recently, the Supreme Court confirmed that, in accordance with ordinary principles of tort liability, directors and officers may owe a duty of care to people other than the corporation they serve, and the objective corporate law standard of care may inform the behaviour expected of them: see *Peoples Department Stores v. Wise*, [2004] 3 S.C.R. 461 at para. 57; *BCE Inc. v. 1976 Debentureholders*, [2008] S.C.R. 560 at para. 44.

Since the corporation is a creature of statute, the principal source of any departure from ordinary principles of tort liability would be the incorporating legislation. But whereas Canadian corporate statutes expressly grant immunity to shareholders, there is no equivalent provision relating to directors, officers, or employees (see e.g. *CBCA*, s. 45(1)). In fact, these statutes implicitly contemplate such personal liability through indemnification provisions that are broad enough to capture obligations owed to third parties (see e.g. *CBCA*, s. 124(1) – "…any civil, criminal, administrative, investigative or other proceeding").

Circumstances that May Give Rise to a Personal Duty of Care

The most promising route to personal liability is through an action for negligence, which would reinforce many of the objectives of the existing voluntary codes and guidelines related to TNCs and human rights. In particular, a common theme of the *OECD Guidelines for MNEs*, the *Guiding Principles on Business and HR*, and the *Voluntary Principles on Security and HR* is the expectation that parent companies, and by extension, their agents, will be proactive in preventing those engaged in their foreign activities from violating human rights. Although tort law is traditionally skeptical of such positive obligations, in recent years Canadian courts have adopted principles that will allow for their recognition in appropriate circumstances.

The most relevant category of such positive obligations is so-called third-party liability, in which it is alleged that the defendant had a duty to prevent a third party from harming the plaintiff. To illustrate this scenario using the facts in *Choc*, the defendant is a director/officer/employee of the parent company, the third party is the security force in the host country, and the plaintiffs are the victims of alleged human rights violations committed by the securities forces.

The recent Supreme Court jurisprudence on third-party liability provides the following lessons for personal liability in the context of TNCs:

1. The director/officer/employee must have actual or imputed knowledge that the security forces' actions would expose the plaintiff to a risk of harm. The nature of the risk posed by the third party will likely have to be specific and clear (see e.g. *Fullowka v. Pinkertons's of Canada*; *Childs v. Desormeaux*);
2. The nature of the relationship between the director/officer/employee and the security forces must be such that the latter cannot be considered wholly autonomous actors (*Childs*);
3. The director/officer/employee must have the capacity to "exert some control" over the risk posed by the security forces. This may be satisfied by the ability to influence the risk environment, rather than the actual perpetrators. The nature of the defendant's role within the TNC or an undertaking on his or her part will be relevant in establishing this capacity (*Fullowka*);
4. There must have been a reasonable expectation and reliance on the part of the Plaintiffs that the director/officer/employee would exercise care with respect to their safety. Again, an undertaking by the Defendant to this effect and his or her role are important factors (*ibid*.)

The ability of the Plaintiffs in the *Choc* to overcome a motion to strike was attributable to the fact that their pleadings hit most of these elements with sufficient particularity. Interestingly, the allegation that the defendants had declared their adoption of the *Voluntary Principles* was among those that the Court considered relevant in terms of proximity. Of course, *Choc* is an action against the parent company, not its directors/officers/employees.

Nevertheless, by convincing the Court that a parent company may have a duty of care to prevent the harmful consequences of activities associated with a foreign subsidiary, the plaintiffs in *Choc* overcame a major hurdle. Given the relationship between personal and corporate liability, it is at least plausible that this duty of care will be extended to directors/officers/employees of the parent company, resulting in a stronger deterrent effect.

To the extent that a shift toward personal liability improves compliance with

human rights, tort litigation may play a role in furthering the UN Sustainable Development Goals. Specifically, it may help ensure the basic conditions necessary for the inclusiveness of the economic development associated with TNCs.

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