

The Increasing Regulation of CSR: Legal and Business Implications

MineAfrica Conference
Canada-Southern Africa Chamber of Business
June 5, 2014

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Overview

- Regulation of Corporate Social Responsibility:
 - Brief History
 - Legal Update
 - What does the Future Hold?
- Legal and Business Implications
- Risk Mitigation Tips
- Value Proposition and Role of Legal Counsel

Backdrop

- Globally, companies face significant risk from governments, local and indigenous communities, NGOs and the general public (as social media and communication capabilities impact corporate brand in real time)
- Risks are overwhelmingly social and environmental
- Risks tend to be higher in developing countries, but significant risks exist everywhere and are increasing because of legal developments
- Enterprises must mitigate and effectively manage CSR risks ongoing to be able to meet legal requirements and avert liability

Regulatory History

- Historic movement from “soft law” (guidelines, recommended practices) to “hard law” (laws, regulations)
- Initially, voluntary practices developed as a result of societal pressures
- **Until relatively recently:**
 - little legislation has been enacted to encode standards of environmental or social conduct, or to prohibit or regulate conduct effectively
 - few court decisions have addressed CSR requirements or liability arising from corporate conduct
- Current trend is toward increasing emergence of hard law as mechanism for regulating corporate responsibility related to social and environmental matters

Regulatory History - Examples

Financiers, Securities Regulators, Legislators, NGOs and Courts have responded to materializing social risk by:

- Measuring corporate conduct against financial performance standards as pre-requisite to project financing (IFC, Word Bank, Equator Principles) and incorporating CSR reporting requirements within contractual financing language
- Securities regulators (e.g. Canada, US, UK, European Union) implementing increasingly more onerous transparency and disclosure obligations for public companies

Regulatory History

- Developing and promoting certification standards for social compliance:
 - ISO 26000 – International Organization for Standardization
 - SA 8000 - Social Accountability International (1997)
 - Global Reporting Initiative



Regulatory History

- Enacting anti-bribery and corruption laws:
[U.S. Foreign Corrupt Practices Act; Dodd-Frank Act (US); Bribery Act (U.K.); Corruption of Foreign Public Officials Act (Canada); Criminal Code Amendment (Bribery of Foreign Public Officials) Act 1999 (Australia)]
- Enacting local laws addressing environmental risk and regulating social impacts
 - South Africa: *Mine Health and Safety Act; National Waters Act; National Environmental Management Act; Black Economic Empowerment Act; Mineral and Petroleum Resources Development Act*
 - Canada: Recent amendments to environmental assessment legislation requiring public engagement and consideration of socio-economic impacts

Legal Update

Recent regulatory developments of significance in Canada include:

1. Ontario Securities Commission requiring significantly increased transparency:
 - June 2011: OSC amended National Instrument 43-101 to require more detailed reporting by mining issuers of potential environmental and community related risks
 - Jan, 2014: OSC opened consultation on proposal to amend National Instrument 58-101 to require public companies to report on gender diversity on corporate boards and in executive ranks
2. Canadian Federal Government (NRCan) is proposing transparency by mining issuers of payments to governments including First Nations governments

Legal Update

3. North American courts have confirmed liability related to social infractions and are awarding (or compelling through settlement) significant damages and personal penalties:
 - Nazir Karigar Case: First Canadian sentencing of an individual to 3 years in prison for bribery of foreign officials
 - Hudbay (Guatemala); Shell (Nigeria); Chevron (Equador): Canadian courts addressing whether parent is responsible for alleged human rights atrocities and environmental impacts of subsidiaries elsewhere
 - Nike Case: Nike was sued by shareholders for making “false and misleading” claims about treatment of workers in foreign jurisdictions; claims turned out to be false with negative effect on share value; California Supreme Court stated that:

“when a business enterprise, to promote and defend its sales and profits, make factual representations about its own products or its own operations, it must speak truthfully.”

Nike settled for \$1.5 million paid to the Fair Labour Association.

Legal Update: Bangladesh Joe Fresh Factory Collapse

- Building collapse - 1,129 dead
- Global outcry prompted garment industry to move to improve suppliers' safety standards
- **Class action law suit**
- Compensation plan for workers: 3 months' salary for 3600 people
- Supply chain management practices for manufacturing companies now under close scrutiny



Legal Update

4. Proposed Amendments to *Canada Business Corporations Act* may

- Expand scope of fiduciary duty of directors by requiring consideration of and reporting on consideration of stakeholder interests
- Require directors to report on and be accountable for the social and environmental impact of company operations
- Require company audits, accounting and compliance mechanisms to be sufficiently robust to prevent and detect bribery (including disclosure of beneficial and nominee owners of company shares, including those outside the reach of the CBCA)
- Encode reporting requirements as to diverse representation on corporate boards

What Does the Future Hold?



"WE DECIDED TO BE MORE TRANSPARENT."

What Does the Future Hold?

- Greater focus on “hard law” to regulate CSR with laws becoming increasingly prescriptive and more stringent
- Regulatory regime for CSR is unfolding in manner similar to that already developed for environmental regulation: Legislated prohibitions against conduct with corresponding penalties, and a prosecutorial regime including potentially severe consequences for corporations, directors and officers will become more prevalent
- Enhanced social media platforms and increasingly sophisticated communication technologies will promote real time global (viral) public scrutiny with corresponding impacts to corporate brand and credibility

Business Implications

- Speed at which CSR risk may materialize in the form of corporate and directors' liability is increasing substantially
- Therefore, necessity of and cost to companies to manage CSR risk will increase
- However, the cost to companies who fail to manage CSR risk where risk crystalizes as liability has now been well researched and demonstrated to be substantial [see research by Enodo Rights: Yousef Aftab and Stephanie Garrett; Report of Rachel Davis and Dr. Daniel Franks; Canadian Business for Social Responsibility (CSBR) and Enodo Rights citing weekly costs of mining shut down from CSR failures]
- Strong corporate governance related to CSR initiatives and risk mitigation strategies are no longer a luxury, but an imperative

Legal Implications

- The legal regime for the regulation of CSR = “strict liability”:
 - command and control (reporting requirements);
 - prohibition and penal sanctions (including exposure to significant financial penalties and possibility of imprisonment);
 - No requirement for proof of intent to commit offence in order for liability to crystalize
- In Canada (and elsewhere), regulatory offences are considered “strict liability offences” [*R. v. Sault Ste. Marie*, [1978] SCC]
- proof of *mens rea* (i.e. intent) is not required; the mere occurrence of the offending event imports liability regardless of intent or fault
- Conviction can be avoided if offender can prove on balance of probabilities that all reasonable care was taken to prevent offence

Risk Mitigation Tips

- CSR risk avoidance involves establishing a strong due diligence defence and prevention program
- Developing appropriate CSR risk mitigation program involves:
 1. Understanding the CSR risks (legal and business) faced by your enterprise
 2. Understanding best practices for averting/addressing risks
 3. Prioritizing risks
 4. Systematically developing corporate policies, governance model; operational practices, strategies and implementation plans (including stakeholder engagement and skills development and training) (i.e. the due diligence program)
 5. Regularly auditing the program to ensure its effective operation
 6. Ongoing corrective action to enhance program and address known risks

Value Proposition and Role of Legal Counsel

- Supplementing “soft law” with toothier “hard law” and emergence of court decisions confirming, imposing and quantifying liability means that lawyers (external and external corporate counsel) have a critical role in supporting companies
- Lawyers, other CSR advisors (government relations, community engagement, environmental consultants) and key corporate personnel must work in an integrated fashion to achieve corporate risk management objectives
- Legal counsel should help design, manage and improve ongoing the due diligence process
- A key role and value proposition is to establish legal privilege to enable best development of the due diligence program and governance model/practices

Value Proposition

Companies who are effective in gaining and maintaining social license with the help of knowledgeable and supportive legal counsel and other CSR advisors will protect themselves, differentiate themselves, and lead in the global market

Thank You

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