MODERN SLAVERY ACT 2015
THE IMPACT ON MULTINATIONAL BUSINESSES

Martin Luff and Thomas Wilson of Vinson & Elkins LLP examine the implications of the Modern Slavery Act 2015 for non-UK businesses and other international human rights obligations for all organisations.

The enactment of the Modern Slavery Act 2015 (2015 Act) made headlines in the UK, but it also generated significant interest in the global community as the latest example of legislative action to address slavery and human rights abuses in commercial supply chains (*see Briefing "Modern Slavery Act 2015 and beyond: putting the spotlight on human rights", www.practicallaw.com/5-620-4611*). Foreign interest has been driven by the extra-territorial reach of the 2015 Act, which applies to UK-based businesses as well as to businesses that are incorporated and headquartered outside the UK but that conduct business within the UK.

The 2015 Act is part of a rapidly evolving patchwork of international guidelines, treaties and legislation that multinational businesses must take into account when drafting and implementing corporate social responsibility (CSR) policies focused on slavery and human rights (*see feature article "Supply chain reporting: complying with the Modern Slavery Act 2015", www.practicallaw.com/6-622-9282*).

This article examines:

- How the 2015 Act affects non-UK businesses.
- Other recent developments in human rights law that multinational organisations, whether based in the UK or outside the UK, must take into account when managing their operations and supply chains.

UK REPORTING REQUIREMENT

As UK-based organisations are busy drafting and publishing their first slavery and human trafficking statements (the statement) under section 54 of the 2015 Act (section 54), many non-UK businesses remain unaware of how, or in what way, the 2015 Act applies to them (*see Focus "Modern Slavery Act 2015: new reporting obligations", www.practicallaw.com/0-614-4097*).

Section 54 requires organisations to report publicly on their efforts to address slavery and human trafficking within their supply chains. Section 54 applies to any commercial organisation, including corporate entities and partnerships, in any sector that supplies goods or services, that carries on a business or part of a business in the UK, and that has a total annual turnover of £36 million or more (*see News brief "Modern slavery: reporting threshold and statutory guidance", www.practicallaw.com/0-618-3116*).

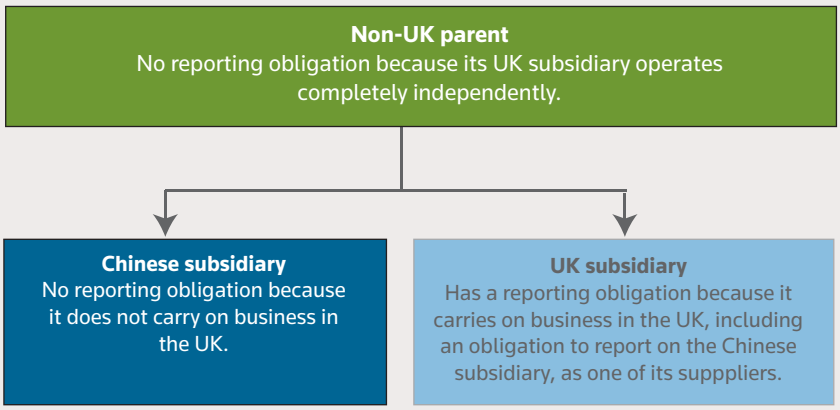
Application to non-UK businesses

The 2015 Act applies irrespective of where an organisation is incorporated or headquartered. Statutory guidance published by the government in October 2015 (the

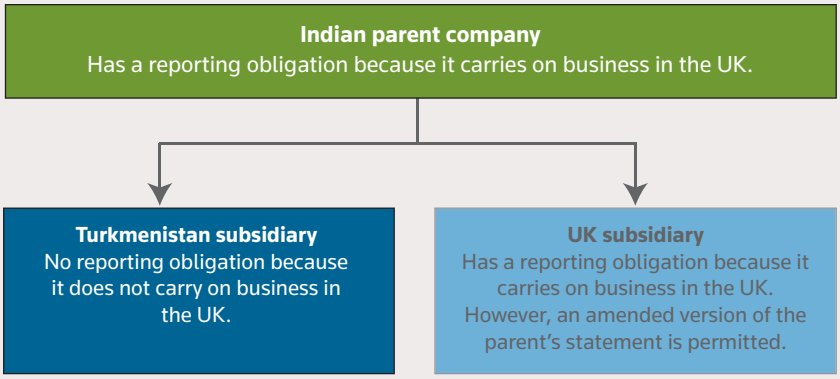
When does the reporting requirement apply?

The examples below illustrate some of the issues that may arise in determining whether a company has an obligation to publish a slavery and human trafficking statement under section 54 of the Modern Slavery Act 2015 (the statement).

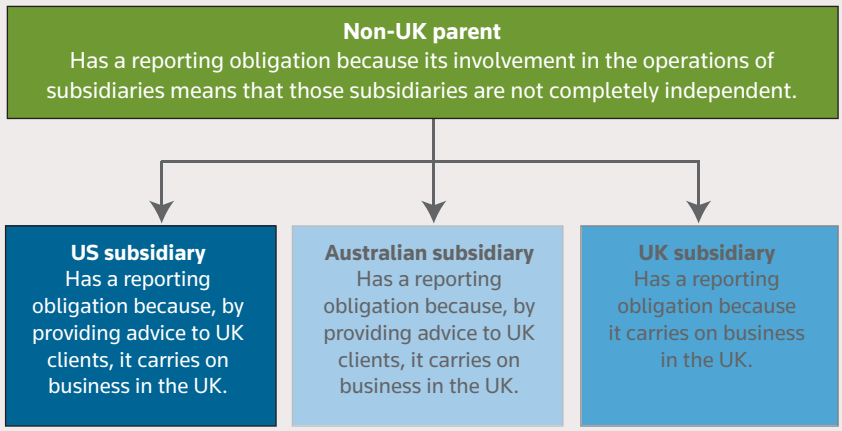
Example 1. A multinational manufacturing group has an annual global turnover in excess of £36 million. Products are manufactured by a Chinese subsidiary that runs the entire group's manufacturing operations. Those products are shipped to various countries around the world. In the UK, the products are sold exclusively through the UK subsidiary, so it will be required to publish a statement. There would be a good argument that the Chinese subsidiary does not have a demonstrable presence in the UK because it is not selling products directly in the UK market. It would therefore not have to publish a statement. However, the Chinese subsidiary would be part of the UK subsidiary's supply chain and therefore its operations would need to be addressed in the UK subsidiary's statement.



Example 2. The parent company is an Indian conglomerate with two subsidiaries, one based in the UK and one incorporated in Turkmenistan. The group's annual global turnover is in excess of £36 million. The Turkmenistan company does no business in the UK and operates independently of the parent and the other subsidiaries, so it is not required to publish a statement. The parent and the UK subsidiary both conduct business directly in the UK so must both publish a statement, although the UK subsidiary may publish an amended version of the parent's statement.



Example 3. An international professional services business with an annual global turnover in excess of £36 million has a UK subsidiary that provides UK advice to its clients. The UK subsidiary will be required to publish a statement. A US subsidiary provides services primarily to US clients but also regularly provides advice to UK clients on US matters. Similarly, an Australian subsidiary provides services primarily to Australian clients but also regularly provides advice to UK clients on Australian matters. This direct provision of services in the UK could trigger the requirement to publish a statement with respect to the US and the Australian subsidiaries.



statutory guidance) emphasises that the key consideration under section 54 is where the organisation carries on its business (*www.practicallaw.com/4-620-3966*). If a foreign organisation carries on a business or part of a business in the UK and meets the £36 million turnover threshold, it is likely that the 2015 Act will apply.

The statutory guidance does not give much detail on what constitutes "carrying on a business or part of a business" and emphasises that the courts will be the final arbiters on this question. But the government expects a commonsense approach to be taken in answering this question.

Organisations that do not have a demonstrable business presence in the UK will not be covered. Similarly, the statutory guidance states that a foreign entity with a UK subsidiary is not covered if the UK subsidiary acts completely independently of the parent and other group companies. In this scenario, the UK subsidiary would be covered but the parent and other group companies would not be covered, assuming that the parent and other group companies do not carry on a business in the UK (*see box "When does the reporting requirement apply?"*).

For each of the entities, both body corporates and partnerships, within a group, consideration will need to be given to whether the entity satisfies each of the requirements of the 2015 Act, that is:

- Does it meet the turnover threshold (*see "Calculating the turnover threshold" below*)?
- Does it supply goods or services?
- Does it carry on a business, or part of a business, in the UK?

Clear lines can rarely be drawn between entities within a corporate group and so it remains to be seen exactly how certain aspects of the test will be applied in practice. In particular, it is not yet clear how the commonsense approach of determining whether an entity is conducting business in the UK will be applied.

A foreign parent with a UK subsidiary will also have to consider whether it has a reporting obligation under the 2015 Act because of the activities of its UK subsidiary. Although the statutory guidance indicates that no reporting obligations will apply if a UK subsidiary acts completely independently of a parent company or other group entities, it is unclear what circumstances would need to exist to establish complete independence.

On its face, complete independence appears to be a very high standard. Some of the factors that might be relevant to this analysis could include: the managerial and administrative independence of the UK subsidiary; whether goods and services supplied by the UK subsidiary are manufactured or produced by group entities other than the UK subsidiary; and the extent to which profits and income generated by the UK subsidiary are transferred to other entities within the group.

Calculating the turnover threshold

The £36 million annual turnover threshold is not limited to turnover in the UK. Turnover for the purposes of the 2015 Act is calculated by reference to the organisation's business activities anywhere in the world and includes the turnover of any subsidiary undertakings, including those operating wholly outside the UK. As a result, foreign businesses with substantial global operations are likely to be caught by the reporting provisions of the 2015 Act even though they might do relatively little business in the UK.

The relatively low turnover threshold, coupled with the fact that the calculation covers global turnover of the organisation and its subsidiaries, means that many multinational businesses are likely to meet this limb of the test. As a result, the question of whether the organisation is carrying on a business or part of a business in the UK is likely to be the most relevant issue for foreign businesses in determining whether the 2015 Act applies to them, and the area in which litigation is perhaps most likely to arise in disputes over whether the 2015 Act applies.

However, the corporate structure of a foreign business could make the turnover issue more relevant. For example, if a multinational company conducts all of its UK-based business through a UK subsidiary that is sufficiently well ring-fenced from the rest of the corporate group, and the UK subsidiary, together with any of its subsidiaries, has an annual turnover of less than £36 million, then the requirements of the 2015 Act would not apply.

Limiting the application of the 2015 Act

In most cases, it is unlikely that companies would go through the administrative hassle and incur the financial cost involved with structuring their businesses in a way that is specifically designed to circumvent the 2015 Act. Furthermore, the potential reputational damage from any publicity over efforts to do this would probably result in a pyrrhic victory for the business. The requirements to produce an annual statement under the 2015 Act are not so onerous as to make the exercise worthwhile in most circumstances.

For some companies, however, making certain adjustments to limit the extent to which the 2015 Act will apply to the wider corporate group may be worthwhile. For example, multinational companies with relatively little business in the UK might want to avoid having to include within the statement details concerning its supply chains that are entirely unrelated to the UK business.

The statutory guidance encourages corporate groups to produce statements that cover non-UK subsidiaries as a matter of good practice to demonstrate a commitment to preventing modern slavery, even if those subsidiaries are not legally required to do so. No doubt, this approach is consistent with the spirit and overall objective of the legislation, and most businesses will want to pursue the laudable goals of the 2015 Act. However, making public disclosures regarding issues within the supply chain can potentially expose a business to a risk of litigation (*see "Potential legal liability" below*).

Publication issues

An organisation that is required to produce a statement must publish the statement on its website. If it does not have a website, it must provide a copy of the statement within 30 days to anyone that makes a written request for it.

Multinational companies that have diverse business operations and a variety of websites for their products and services may need to give some thought to where the statement should be published. The 2015 Act states that an organisation must include a link to the statement in a prominent place on the homepage of its website. The statutory guidance indicates that where there are multiple websites for an organisation, the statement should be published on the websites relating to the organisation's UK business.

If more than one company in a group is required to produce a statement, a single joint statement may be produced, provided

that it sets out the steps that each entity has taken. If the parent company and subsidiaries are all required to make statements, they may produce one joint statement, provided that the parent includes in its joint statement the steps that each of its subsidiaries have taken as well.

The sanctions for non-compliance include the granting of an injunction to compel a report. A subsequent failure to comply might result in contempt of court proceedings and a fine. Organisations also risk reputational damage if they fail to comply (*see box "Best practice compliance"*).

Best practice compliance

Best practice for non-UK businesses to ensure compliance with the Modern Slavery Act 2015 (2015 Act) would be to:

- Review the corporate and operational structure to confirm which entities are carrying on a business in the UK and assess whether turnover thresholds under the 2015 Act have been met.
- Consider retaining a specialist external supply chain auditor to monitor compliance, or appoint a compliance monitor from within the organisation or from an outside source, such as a law firm.
- Ensure that there is a company-wide policy on modern slavery and how to prevent it, and that appropriate personnel are trained on that policy.
- Confirm that suppliers, both within and outside the corporate group, are aware of what is expected in terms of compliance standards.
- Ensure consistency with other company policies that might affect modern slavery issues, such as those related to bribery and corruption.
- Identify high-risk areas, both in terms of geographic location and industry sector, on which to focus anti-slavery efforts.

HUMAN RIGHTS OBLIGATIONS

For multinational companies, whether they are headquartered in the UK or outside the UK, the 2015 Act is just one of a number of international human rights obligations affecting their global operations (*see Briefing "Human rights reporting: the tip of the iceberg", www.practicallaw.com/8-589-4769*). The adoption of CSR policies and statements has become commonplace, driven in part by the expansion of human rights laws as well as the increased publicity of human rights abuses through social media and the activities of non-governmental organisations (NGOs) and other advocacy groups.

Many of the recent legislative developments focus on transparency in supply chains and public disclosure of human rights and slavery issues but do not create affirmative legal obligations to eliminate or prevent human rights abuses. Rather than have governmental bodies policing compliance of substantive legal obligations, it appears that the current legislative strategy is to create disclosure obligations with the expectation that public awareness and the potential adverse impact on a business's reputation will be the most effective way of combatting human rights abuses. The 2015 Act is the latest example of this trend.

United Nations

Since its inception, one of the United Nations' (UN) principal concerns has been to address global human rights issues. The UN adopted the Universal Declaration on Human Rights in 1948. In 1966 it ratified two treaties, the International Covenant on Civil and Political Rights, and the International Covenant on Economic, Social and Cultural Rights, both of which created a binding commitment on signatory states to protect human rights and established a body to hear complaints. Together, these three documents are known as the International Bill of Human Rights.

Over the subsequent decades, there was a growing recognition that businesses, rather than states alone, can and should play a critical role in combating modern human rights abuses, such as slavery and the exploitation of indigenous peoples.

In 2005, the UN appointed Harvard Professor John Ruggie as a Special Representative tasked with developing a set of standards to guide multinational companies in managing human rights issues. This culminated in the UN Human Rights Council's Guiding Principles on Business and Human Rights (the guiding principles), which were endorsed by the UN in 2011 (*see Briefing "Business and human rights: the UK's action plan", www.practicallaw.com/6-546-1286*).

The guiding principles established a "protect, respect and remedy" framework for all businesses to identify and address human rights abuses. The guiding principles are not legally binding obligations but are, instead, intended to appeal to businesses' sense of social responsibility and to call on governments to enact domestic legislation to protect human rights and establish effective remedial measures.

The guiding principles have three pillars, the second of which is most relevant to multinational businesses:

- States have a duty to protect against human rights abuses within their territory or jurisdiction which are perpetrated by third parties, including business enterprises.
- Businesses have a responsibility to respect human rights, avoid infringing those rights and address any potential adverse effects that their operations may have on human rights.
- States must take appropriate steps to ensure, through judicial, administrative, legislative or other appropriate means, that when human rights abuses occur within their territory or jurisdiction, that those affected have access to effective remedies.

The guiding principles reflect the rights described in the International Bill of Human Rights and the International Labour Organization's Declaration on Fundamental Principles and Rights at Work. Under the second pillar above, businesses should avoid direct violations of human rights and prevent or mitigate any indirect negative effects of their operations.

Adherence to the guiding principles requires a business to: create a policy stating its commitment to meet its responsibilities to protect human rights; establish a due diligence process to identify, prevent and mitigate effects on human rights; and establish a remediation process to address violations if they occur. The guiding principles also emphasise that human rights policies should be prepared with the assistance of relevant experts and approved by the most senior levels of the business, such as the board of directors.

While the guiding principles do not impose direct legal obligations on businesses or provide a private right of action against companies that violate the standards, many large businesses have adopted CSR and human rights policies that closely mirror the guiding principles.

Domestic human rights laws

The legislative trend in several jurisdictions around the world has moved towards the enactment of domestic laws that directly address human rights in the context of international commercial operations and the supply chain. The 2015 Act is the latest example of that trend, but laws that address similar issues have come into force in other jurisdictions, or are currently in the legislative pipeline.

In the US, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 requires public corporations that rely on conflict minerals (including tin, tantalum, tungsten and gold) in their products to conduct due diligence to determine whether their conflict mineral supply chains are contributing to armed conflict in the Democratic Republic of the Congo and neighbouring countries. Corporations are required to file public reports describing their due diligence efforts and findings with the US Securities and Exchange Commission (SEC). However, specific parts of these SEC reporting regulations have been challenged in the US federal court and have been found to be unenforceable.

The EU is in the process of developing its own conflict minerals regulations. The EU's current proposal will require all importers of conflict minerals to conduct a due diligence review of imports from any conflict-affected area, not just those within Africa, and importers may be required to obtain third-party audits from their smelters and refiners to confirm how conflict minerals are sourced. The EU's conflict mineral regulations are working their way through the EU law-making process, with updates likely to come in 2016.

Recent legal developments extend beyond conflict minerals. For example, under California's Transparency in Supply Chains Act of 2010, a corporation doing business in the state of California that has annual worldwide gross receipts that exceed $100 million is required to publicly report its efforts in evaluating and addressing risks of human trafficking and slavery within its supply chains, including auditing its suppliers for compliance. Similarly, the 2015 Act is not restricted to a particular industry or sector.

Potential legal liability

In-house counsel and corporate compliance officers may be concerned about the unanticipated negative consequences of publishing CSR and human rights policies. In some cases, policies and public statements may serve to prove a company's knowledge of the potential for violations of international human rights in its foreign operations (*see box "Nestlé's legal liability"*).

Apart from the Nestlé litigation, there is currently little evidence that there is likely to be a surge, or even a noticeable trend, of companies being exposed to greater liability as a result of their CSR and human rights policies.

In fact, with the enactment of laws such as the 2015 Act and the California Transparency in Supply Chains Act, businesses are now increasingly under a legal obligation to make public statements on these issues.

The key to avoiding and managing liability will be the company's ability to implement its policies effectively and take positive steps to address human rights abuses in its own operations and its supply chains. A disconnect between a company's written policies and the steps that it is actually taking in the field is likely to increase potential liability because, for example, NGOs and individual claimants can more easily prove knowledge on the part of a company as well as show a demonstrable difference between a company's statements on a particular issue and the steps that it has actually taken, or the lack of steps.

For these reasons, it is all the more important for businesses to follow through and take real and meaningful action in meeting the standards that they set for themselves in their policies and mission statements.

Nestlé's legal liability

Recent litigation in the US federal courts against Nestlé USA Inc under the US Alien Tort Statute illustrates why particular care must be taken in drafting and implementing corporate responsibility policies in a way that satisfies applicable legal obligations without increasing potential exposure to liability for human rights violations in foreign supply chains.

The US court held that a group of non-US claimants could pursue a legal action against a US-based entity in the US federal court system in relation to farms in its supply chains that were allegedly engaged in various unlawful practices, including the use of slave labour. The company's public commitments and due diligence efforts to combat slave labour in the cocoa industry were cited by the claimants as evidence of Nestlé's knowledge of human rights abuses in the Ivory Coast. The Ninth Circuit Court of Appeals ruled that the claimants could pursue their claims under the Alien Tort Statute, and in January 2016, the US Supreme Court denied Nestlé's petition for review (*Nestle USA Inc v John Doe No 15-349*).

COMPLIANCE STRATEGY

There are a number of steps that multinational organisations can take to ensure compliance with their human rights obligations.

Develop a team

An internal team should be created to develop the company's human rights policies, organise its due diligence efforts and oversee its responses. The team should have a designated leader who reports directly to the highest level of management. The team should include members from the legal, compliance, supply chain management, HR and any other relevant departments.

Educate

The company should educate itself on the human rights abuses that are of particular relevance to its industry and the regions in

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which it operates by seeking both internal and external input.

Internal expertise may include employees with direct knowledge of field conditions, supply chain managers with knowledge of the company's business partners, legal counsel with knowledge of international compliance laws and HR professionals with knowledge of the company's workforce.

Outside expertise might include individuals with knowledge of specific human rights issues as well as knowledge of regional and industry issues. Experts may include academics, NGOs, trade groups and other businesses, including competitors, that are tackling the same issues. Importantly, input should also be sought from local communities in regions in which the business operates.

Using this information, the team should be responsible for educating the company's management, employees and business partners about the human rights issues that it faces.

Assess and prioritise

Large international businesses are multifaceted and can be located in many countries. The scale of the operations and the variety of human rights issues to be addressed can make the task appear daunting. With advice from its experts, the team should develop a plan that prioritises combating the most egregious human rights abuses, such as slavery or child labour. The company should also be particularly sensitive to any potential human rights issues that may arise when working in high-risk regions.

Commit

The company should not only fully commit to its goals, policies and procedures but should, to the extent possible, require its business partners to commit to the same standards. This can be done most effectively at the procurement and contracting stage, with a preference for doing business with those parties that are demonstrably committed to addressing human rights abuses.

Audit

The company should continually audit its efforts to address human rights abuses and assess how successful it is in addressing these issues. Effective due diligence processes that gather meaningful data are critical to the success of an audit process. Although an audit process will need to be tailored to the specific circumstances, audits will typically include written questionnaires and disclosures, as well as field observations and interviews from stakeholders and field employees. To the extent possible, the due diligence process should cover suppliers and other business partners.

Address

The company should address any human rights abuses that it uncovers. The actions to be taken may include changing its operations, its business partners or even the countries in which it operates. The company should enable its employees to address and prevent human rights abuses directly. This might include, for example, allowing field employees to order a work stoppage if human rights abuses are uncovered.

Remedy

The company needs to develop procedures to remedy any human rights abuses in which it could be considered complicit, whether directly or indirectly. The procedures need to be open and available to anyone whose human rights may be adversely affected, including local stakeholders and employees of the company's business partners. Consideration should be given to the appropriate mechanism for any remediation or grievance procedure.

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