



Directors' Duties and Corporate Social  
Responsibility under German Law – Is Tort  
Law Litigation Changing the Picture?

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## ABSTRACT

This article discusses the right and a potential duty of directors to pursue CSR policies under German law. It first explains the two main duties of directors: to make sure that the company complies with its legal obligations, which has been broadly interpreted in Germany to include the duty to extend to domestic and foreign subsidiaries' compliance with the law, and to act for the (economic) benefit of the company. CSR policies will often only come under the second duty, which means that they can be pursued if they are economically beneficial. However, acting in order to benefit the company also means the avoidance of unnecessary risk, including the risk of tort law liability. This article discusses how recent tort law development towards a duty of care of parent companies for employees of their subsidiaries, and perhaps even victims of their subsidiaries' operations, as triggered by the English landmark case of *Chandler v Cape*, has created risks for parent companies that affect the duty of their directors to establish a corporation-wide system of prevention. It is argued that those liability risks are substantive in amount but uncertain due to the early state of case law, with a number of relevant cases pending at this moment; which allows directors a certain margin of appreciation. The article concludes that the tort law development has certainly strengthened the *right* of directors to pursue a CSR policy that avoids liability, while a corresponding *duty* of directors may arise and intensify with the influx of more transnational tort law cases and, in particular, with judgments in favour of victims of torts committed in the course of operations of transnational corporations in developing countries.

## 1. INTRODUCTION

The discussion on directors' duties and corporate social responsibility (CSR) has come a long way. At the outset, it centred around the question of whether or not the directors of a company were allowed to pursue CSR although this might be less profitable than ruthless (but lawful) behaviour. In the meantime, the tone has shifted towards a potential duty of directors to pursue CSR goals. In this article, several developments in German law (and beyond) shall be discussed, which together may have changed, or have the potential to change, the picture: case law relating to directors' duties under the legality principle, in particular in the context of transnational corporations with subsidiaries in developing countries, and developments in tort law that may have an impact on the duty to avoid unnecessary risks for the benefit of the company. Combined, they have the potential not only to justify the pursuance of CSR but they may even pave the way towards a duty to include at least aspects of CSR into the policy and operations of the corporation.

### 1.1. TWO STRANDS OF DIRECTORS' DUTIES

Directors' duties are duties that are owed to the company, not to third parties. Thus, a breach of directors' duties does not normally lead to external liability but to a claim of the company against the director. That claim must, of course, be based on the damage that the company suffered from the breach, and that damage may consist of liability towards victims of a tort. It could, however, also be damage that consists in fines for unlawful behaviour.

Directors' duties are legally defined for the public limited company (*Aktiengesellschaft*). Under § 93 para. 1 *Aktiengesetz* (AktG), in conducting business, the members of the management board shall employ the care of a diligent and conscientious manager. They shall not be deemed to have violated the aforementioned duty if, at the time of taking the entrepreneurial decision, they had good reason to assume that they were acting on the basis of adequate information for the benefit of the company.

In the following, the article deals with two types of directors' duties: the legality principle and the duty to act for the benefit of the company.

### 1.2. THE LEGALITY PRINCIPLE

Regardless of the potential economic benefit of unlawful behaviour, directors always have the duty to comply with legal obligations.<sup>1</sup> This would, of course, include legal obligations relating to corporate social responsibility. For example, bribery would be a breach of directors' duties even if the bribe in question secures beneficial business.<sup>2</sup> The legality principle has seen significant development in recent years that is of great relevance in the context of transnational corporations.

#### 1.2.1. CONTROL OF SUBSIDIARIES

The legality principle has two elements: First, the directors themselves are required to act in accordance with the law, and second, they have to ensure compliance with the law by their subordinates; which triggers the question of whether the directors and staff of subsidiaries are subordinated to the directors of the parent company.<sup>3</sup> In principle, the

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<sup>1</sup> See German Federal Supreme Court (*Bundesgerichtshof*; hereinafter: BGH) NJW 2010, 3458, 3460. See also Dirk A Verse, 'Compliance im Konzern' [2011] *Zeitschrift für das gesamte Handelsrecht und Wirtschaftsrecht* 401, 405.

<sup>2</sup> See LG Munich I, *Neue Zeitschrift für Gesellschaftsrecht* 2014, 345, 346; Eike Bicker, 'Compliance – organisatorische Umsetzung im Konzern' [2012] *Die Aktiengesellschaft* 542; Gerald Spindler, '§ 93' in Wulf Goette, Mathias Habersack and Susanne Kalss (eds), *Münchener Kommentar zum Aktiengesetz*, 4<sup>th</sup> ed (CH Beck 2014) margin notes 91ff. For an outdated view in a slightly different context see BGH NJW 1985, 2405.

<sup>3</sup> On the related controversial discussion see Uwe H Schneider and Sven H Schneider, 'Konzern-Compliance als Aufgabe der Konzernleitung' [2007] *Zeitschrift für Wirtschaftsrecht (ZIP)* 2061 vs. Verse, *supra* note 1, at 411ff.

majority of authors agree with such a corporation-wide coverage of the directors' duties and argue that the directors of the parent company are required to establish a corporation-wide compliance system; whereas the details of such a system may differ from one corporation to the next and be subject to some discretion. This is despite the recognition of the legal separation of the parent company and its subsidiaries, and the reason for the duty to establish a corporation-wide compliance system may also be seen in the risk that a breach of law by the subsidiary may affect the assets of the parent company.<sup>4</sup> Moreover, one may refer to the voluntary German Corporate Governance Code (*Deutscher Corporate Governance Kodex*),<sup>5</sup> which presents essential statutory regulations for the management and supervision of German listed companies and contains, in the form of recommendations and suggestions, internationally and nationally acknowledged standards for good and responsible corporate governance, formulated under the heading 'Management Board': 'The Management Board ensures that all provisions of law and the enterprise's internal policies are abided by and works to achieve their compliance by group companies (compliance).'<sup>6</sup>

#### 1.2.2. THE TRANSNATIONAL DIMENSION

Arguably, the duty to establish a corporation-wide compliance system extends to foreign subsidiaries. This was confirmed in the *Neubürger* decision of the Landgericht Munich I.<sup>7</sup> Mr Neubürger was the financial director of Siemens AG, the parent company of innumerable subsidiaries worldwide. During his term of service, a corporation-wide system of corruption existed, in the context of which a Nigerian subsidiary of Siemens AG won government contracts through bribery. The discovery of that system led not only to an immense loss of reputation but also to fines imposed on Siemens AG by the United States Securities and Exchange Commission (SEC). Moreover, Siemens AG paid an estimated €474 million to the law firm they had commissioned to investigate the

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<sup>4</sup> See, e.g., Holger Fleischer, 'Corporate Compliance im aktienrechtlichen Unternehmensverbund' [2008] *Corporate Compliance Zeitschrift* 1, 6. See also Verse, *supra* note 1, at 407ff., who however argues that the duty to ensure compliance with the law of subsidiaries does not stem from the legality principle but from the duty to act to the benefit of the company; which would mean that the directors could decide to let the subsidiary engage in unlawful activities if they are to the benefit of the company; *ibid.*, 411ff.

<sup>5</sup> The German Corporate Governance Code is referred to in § 161 AktG. It follows the principle of comply or explain. Thus, listed corporations do not have to follow the recommendations and suggestions but they have to lay open if they do not do so and explain why they choose not to adhere to particular recommendations and suggestions.

<sup>6</sup> GermanCorporateGovernanceCode,2005, <[www.dcgk.de//files/dcgk/usercontent/en/download/code/2015-05-05\\_Corporate\\_Governance\\_Code\\_EN.pdf](http://www.dcgk.de//files/dcgk/usercontent/en/download/code/2015-05-05_Corporate_Governance_Code_EN.pdf), principleG 4.1.3.> accessed 1 September 2017.

<sup>7</sup> LG Munich I, *supra* note 2.

details of the corruption system. Of that amount, Siemens AG reclaimed a part of €15 million from Mr Neubürger, arguing that he breached his duties under § 93 para. 2 AktG, thereby causing damage to Siemens AG, and Siemens AG succeeded in the Landgericht Munich I.

The court argued that the directors' duties include the establishment of a supervision system by which breaches of the law are prevented. The details of that requirement depend on the type and size of the enterprise, the relevant legal provisions, the geographical situation and previous suspicious situations. In the instant case, the court held that the directors, amongst them Mr Neubürger, had not taken any measures to improve the compliance management system of Siemens AG despite repeated hints towards its lack of effectiveness, and the lacking reliability of the regional compliance officer but rather covered the responsible members of staff and misled the supervisory board.

The decision was the subject of a controversial debate in academic literature.<sup>8</sup> Mr Neubürger appealed but reached an out-of-court settlement with Siemens before the trial started (and committed suicide shortly after). Thus, the decision was never overruled, and it would not be wise for a director to ignore it.

### 1.2.3. THE PRACTICAL RELEVANCE OF THE LEGALITY PRINCIPLE

As mentioned above, a breach of the directors' duties does not give rise to damage claims by external victims<sup>9</sup> but only by the company itself, which means that they will only influence the behaviour of directors if there is a risk that the company will enforce the claim. The relevant body is the supervisory board (*Aufsichtsrat*). Here, another landmark decision has increased that risk drastically. In the case of *ARAG v Garmenbeck*, the BGH decided that the members of the supervisory board who do not bring such a claim on behalf of the company incur liability for breach of their own duties.<sup>10</sup> That decision has changed the picture in that claims against directors have been brought more frequently ever since.<sup>11</sup> For example, the supervisory board of Volkswagen AG is currently considering to sue

<sup>8</sup> For critique, see Gregor Bachmann, 'Anmerkung zum Urteil des LG München I vom 10.12.2013 - 5 HK o 1387/10 - Zur Haftung des Vorstands für Mängel des Compliance-Systems' [2014] *Zeitschrift für Wirtschaftsrecht* 579; Walter G Paefgen, '"Compliance" als gesellschaftsrechtliche Organpflicht?' [2016] *Wertpapier-Mitteilungen* 433.

<sup>9</sup> In particular, § 93 AktG is not a statute whose breach would give rise to the tort of breach of a statutory duty under § 823 para. 2 BGB, see, e.g., Spindler, *supra* note 2, margin note 309.

<sup>10</sup> BGH, NJW 1997, 1926.

<sup>11</sup> See Tim Drygala, Marko Staake and Stephan Szalai, *Kapitalgesellschaftsrecht* (Springer 2012) § 21 margin note 97. In academic writing, in contrast, there seems to be a trend to weaken the meaning of *ARAG v Garmenbeck* and to allow the supervisory board some discretion. For an overview of the debate see Jens Koch, 'Die schleichende Erosion der Verfolgungspflicht nach ARAG/Garmenbeck' [2014] *Neue Zeitschrift für Gesellschaftsrecht* 934.

the directors of Volkswagen AG and Audi for at least negligent omission to prevent 'Dieselgate'.<sup>12</sup>

Moreover, it should be mentioned that coverage of directors' and officers' (D&O) insurance has been restricted in 2009. Under § 93 para. 2 sent. 3 AktG, insurance contracts must provide for a director's contribution of at least 10% of the damage up to at least 1.5 times the fix annual salary. This was explicitly meant to create incentives for directors to act responsibly.<sup>13</sup>

#### 1.2.4. THE EXTENT OF AND LIMITATIONS TO THE LEGALITY PRINCIPLE

##### (a) Statutory obligations

Liability under the legality principle requires a breach of law, which in transnational situations may often mean the breach of the law of the host state of the subsidiary.<sup>14</sup> Thus, the legality requires the directors of parent companies to ensure compliance with local laws; which, often do not require 'socially responsible' behaviour. It should, however, be noted that some of the 'classical' CSR issues, such as the lack of a working fire protection system, as in the case of the Ali Enterprises factory fire,<sup>15</sup> are in breach of local laws. Moreover, a number of developing countries avail of modern environmental laws<sup>16</sup> (which are, however, often not enforced).

In contrast, there is little doubt that soft law, and even international soft law, does not count as 'law' in this sense but would rather be classified as an emanation of 'good morals'; and clearly, there is no obligation under German company law to comply with good morals.<sup>17</sup> Thus, there is no duty to comply with CSR instruments such as the OECD Guidelines,<sup>18</sup> the Global Compact<sup>19</sup> or the 'Protect, Respect and Remedy Framework'<sup>20</sup>

<sup>12</sup> See Kristina Gnirke, 'Winterkorn und Stadler droht Millionenforderung' (*Spiegel online*, 4 April 2017) <[www.spiegel.de/wirtschaft/unternehmen/volkswagen-martin-winterkorn-und-rupert-stadler-droht-millionenforderung-a-1141287.html](http://www.spiegel.de/wirtschaft/unternehmen/volkswagen-martin-winterkorn-und-rupert-stadler-droht-millionenforderung-a-1141287.html)> accessed 14 June 2017.

<sup>13</sup> See the report of the legal committee (*Bericht des Rechtsausschusses*), *Printed Matters of the German Bundestag (Bundestags-Drucksache)* 16/13433, 11

<sup>14</sup> See also Michael Kort, 'Gemeinwohlbelange beim Vorstandshandeln' [2012] *Neue Zeitschrift für Gesellschaftsrecht* 926, 927.

<sup>15</sup> On which see *infra*, at 3.1.2.

<sup>16</sup> See, e.g., the case of *Vedanta*, *infra* at 3.1.1., that was concerned with the breach of Zambian environmental legislation; which caused harm to neighbouring communities.

<sup>17</sup> Kort, *supra* note 14, at 929; Wolfgang Hölters, '§ 93 AktG' in Wolfgang Hölters (ed), *Aktiengesetz*, 2nd ed (CH Beck 2014), margin note 70.

<sup>18</sup> OECD Guidelines for Multinational Corporations as first adopted in 1976, <<http://mneguidelines.oecd.org/text>> accessed 1 September 2017.

<sup>19</sup> "Homepage | UN Global Compact" (*Homepage | UN Global Compact*) <[www.unglobalcompact.org](http://www.unglobalcompact.org)> accessed August 15 2017.

<sup>20</sup> John Ruggie, 'Protect, Respect and Remedy: a Framework for Business and Human Rights', (UN doc A/HRC/8/5, 7 April 2008) <[www.reports-and-materials.org/Ruggie-report-7-Apr-2008.pdf](http://www.reports-and-materials.org/Ruggie-report-7-Apr-2008.pdf)> accessed 1 September 2017.

and the 'Guiding Principles on Business and Human Rights'<sup>21</sup> as such, that is, if they have not found entry into the law, for example, through open-ended norms,<sup>22</sup> or into the internal regulation of the corporation, in particular due to subscription to, for example, the Global Compact.

*(b) Internal regulation*

In the context of directors' duties, the notion of 'legal obligations' goes beyond obligations stemming from statutory law. It also includes the internal regulation of the corporation, thus the 'law of the company'.<sup>23</sup> The directors are bound by the by-laws as far as the subject of the enterprise and the aims and objectives of the corporation are concerned. This may of course include the aim to be a social and environmentally friendly corporation, which may be expressed in the adoption or signature of soft law instruments, such as codes of conduct. Thus, compliance with codes of conduct to which the corporation has signed up would seem to come within the scope of the legality principle. The same applies to compliance with internal guidelines that have been adopted or consented to by the competent bodies of the corporation, as compliance with such regulation is in the interest of the corporation. In contrast, the directors would not be forced, under the legality principle, to enforce guidelines that they have set up themselves but which have not become part of the internal regulation of the corporation. Again, breach of internal regulation will only be actionable if it caused damage to the corporation.

#### 1.2.5. SUMMING UP

The legality principle is able to cover CSR issues that are expressed in legal obligations, including those established in the host states of subsidiaries. In contrast, it has no significance for any duty or right of directors to pursue CSR policies beyond the law, including the internal regulation of the company.

#### 1.3. THE BENEFIT OF THE COMPANY

Where there is no legal obligation, the directors have the duty to act for the benefit of the company. Here, they enjoy the discretion that is

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<sup>21</sup> John Ruggie, 'Guiding Principles on Business and Human Rights: Implementing the United Nations "Protect, Respect and Remedy" Framework', (UN doc A/HRC/17/31, 31 March 2011) <[www.ohchr.org/documents/issues/business/A.HRC.17.31.pdf](http://www.ohchr.org/documents/issues/business/A.HRC.17.31.pdf)> accessed 1 September 2017.

<sup>22</sup> On which, see Carola Glinski, 'The Ruggie Principles, business human rights self-regulation and tort law: Increasing standards through mutual impact and learning' (2017) 15 *Nordic Journal of Human Rights* 15, concerning the relationship between the Ruggie Framework and Guiding Principles, tort law and transnational private regulation, with further references.

<sup>23</sup> See Holger Fleischer, '§ 93 AktG', in Gerald Spindler and Eberhard Stolz (eds), *Kommentar zum Aktiengesetz*, 3rd ed (CH Beck 2015) margin notes 21f.



commonly referred to as the business judgment rule. Actually, the second sentence of § 93 para. 1 AktG, according to which the directors shall not be deemed to have violated the aforementioned duty if, at the time of taking the entrepreneurial decision, they had good reason to assume that they were acting on the basis of adequate information for the benefit of the company, has not always formed part of German law. It was introduced in 2005 in the aftermath of the above-mentioned *ARAG* decision of the BGH<sup>24</sup> in order to clarify that directors are not liable for the lack of success of the company but only for imprudent decisions in breach of the business judgment rule.<sup>25</sup> The business judgment rule was meant to be a codification of the *ARAG* decision. Although it was only explicitly codified in the law on public limited companies, the same principles apply for private limited companies under § 43 *Gesetz betreffend die Gesellschaften mit beschränkter Haftung* (GmbHG) and other companies, as the legislator has mentioned expressly in the explanations on the draft legislation.<sup>26</sup>

CSR strategies will often have the potential benefit the company, an issue that is commonly discussed as the ‘business case of CSR’.<sup>27</sup> Key words are market advantages through advertising with CSR, employees’ satisfaction leading to reduced fluctuation, good relationship with government and the avoidance of scandals that might lead to loss of reputation or consumer boycotts.<sup>28</sup> The latter aspect is currently gaining momentum through the CSR Reporting Directive 2014/95/EC,<sup>29</sup> which will force big corporations to lay open their CSR policies.<sup>30</sup>

In connection with the business judgment rule, such potential advantages of socially responsible behaviour may often justify a CSR policy,<sup>31</sup> although this is not necessarily the case, for example, where there are no end-users involved, as in the extraction industry, or where end-users are insensitive to the well-being of people in the host states of the

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<sup>24</sup> And a follow-on decision in the case of *Siemens AG v Nold*, BGH NJW 1997, 2599.

<sup>25</sup> See Spindler, *supra* note 2, margin note 8.

<sup>26</sup> See *Printed Matters of the German Bundestag* 15/5092, 12. See, e.g., BGH NJW 2010, 3458.

<sup>27</sup> On which see, e.g., Dennis J Aigner, ‘Corporate Social Responsibility and Financial Performance’ in Ronny Manos and Israel Drori (eds), *Corporate Responsibility* (Palgrave & Macmillan 2016) 11.

<sup>28</sup> Examples for financial loss resulting from scandals are Nike and Shell (in the context of the oil platform Brent Spar), see, e.g., Menno T Kamminga, ‘Company Responses to Human Rights Reports: An Empirical Analysis’ [2016] *Business and Human Rights Journal* 95, 101.

<sup>29</sup> Directive 2014/95/EU amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups, OJ 2014 L 330/1.

<sup>30</sup> See, e.g., Peter Hommelhoff, ‘Nichtfinanzielle Ziele in Unternehmen von öffentlichem Interesse’ in Reinhard Bork, Godehard Kayser and Frank Kebekus (eds), *Festschrift für Bruno M. Kübler zum 70. Geburtstag* (CH Beck 2015) 291.

<sup>31</sup> See, eg, Hölter, *supra* note 17, margin note 70.

production.<sup>32</sup> If there is no possible benefit, most authors would deny the directors' right to pursue a CSR policy.<sup>33</sup>

Certainly, it would be difficult to argue in favour of a *duty* to act socially responsibly for the benefit of the company (given the undeniable costs of CSR), unless in the individual case, it is obvious that pursuing a CSR strategy – to what extent? – *will* be more beneficial to the corporation than not caring about CSR.

Another aspect of the duty to act for the benefit of the company is the duty to avoid unnecessary risks, including the unnecessary liability to third parties.<sup>34</sup> The duty to avoid unnecessary liability risks requires consideration of the extension of the risk and the likelihood of its materialisation.<sup>35</sup> Thus, special care is required where a business decision puts the whole enterprise at risk.<sup>36</sup>

## 2. CHANGES THROUGH TORT LAW LITIGATION?

Tort law litigation against transnational corporations and even against the dominant purchaser in a supply chain is the topic of the day, and corporations from, for example, the oil business and the extracting industry are facing litigation by victims of human rights abuses and environmental degradation in several jurisdictions; which may lead to high damage payments that affect the success of the corporation. Thus, in the following, the recent development in tort litigation is analysed and put into context with the directors' duty to avoid unnecessary risk. It should be mentioned that liability risks may also stem from other areas of law, for example from securities law or from unfair commercial practices law, where a corporation does not keep its CSR promises. These are, however, not subjects of this article.

### 2.1. NOVELTIES IN TORT LITIGATION

#### 2.1.1. TORT LAW LIABILITY IN CORPORATE STRUCTURES

Tort law litigation related to – broadly speaking - the parent company's liability for damage suffered by employees and neighbours of

<sup>32</sup> On loss of reputation that may or may not lead to financial loss, see Lars Klöhn and Klaus Ulrich Schmolke, 'Unternehmensreputation (Corporate Reputation)' [2015] *Neue Zeitschrift für Gesellschaftsrecht* 689.

<sup>33</sup> See, eg, Kort, *supra* note 14, at 929. For a deviating position, see Olaf Müller-Michaels and Wiebke Ringel, 'Muss sich Ethik lohnen?' [2011] *Die Aktiengesellschaft* 101.

<sup>34</sup> See, eg, Spindler, *supra* note 2, margin note 67; OLG Jena, *Neue Zeitschrift für Gesellschaftsrecht* 2001, 86

<sup>35</sup> Dirk Kocher, 'Zur Reichweite der Business Judgment Rule' [2009] *Corporate Compliance Zeitschrift* 215, 217. On the criterion of likelihood, see OLG Jena, *Neue Zeitschrift für Gesellschaftsrecht* 2001, 86; Egon Kust, 'Zur Sorgfaltspflicht und Verantwortlichkeit eines ordentlichen und gewissenhaften Geschäftsleiters' [1980] *Wertpapier-Mitteilungen* 758, 761.

<sup>36</sup> See Spindler, *supra* note 2, margin notes 54f.

subsidiaries in developing countries has been discussed in academic writing for a long time<sup>37</sup> but has been fuelled by the English landmark case of *Chandler v Cape*,<sup>38</sup> although, ironically, the case was purely domestic as both the parent company and the subsidiary were domiciled in England. Nevertheless, the case was seen as a breakthrough in imposing liability on parent companies for problems that occurred in the realm of the subsidiary, and academics as well as practitioners immediately made the link to the classical problems of corporate liability for disasters in developing countries.

The case concerned an English worker, Mr. Chandler, who during work for Cape Products over a longer period of time was exposed to asbestos dust. Cape Products was a wholly owned subsidiary of Cape plc. Both companies were situated in the UK. Cape plc had control over the asbestos business carried out by the subsidiary in the sense that the products were manufactured in accordance with Cape's product specifications. The separate administration of Cape Products was originally approved of by Cape plc on the condition that Cape products would be run 'in accordance with company policy'. Cape plc had a group medical advisor employed, who was responsible for the health and welfare of all employees within the corporation (a 'flying' doctor) and also a scientific officer who was responsible for trying to find methods to suppress asbestos dust. Cape plc knew that the system of work at Cape products was defective. When Mr. Chandler became ill, Cape Products no longer existed. Consequently, Mr. Chandler sued the parent company, Cape plc, instead.

The court found Cape plc liable towards Mr. Chandler under the tort of negligence, relying on a wide interpretation of the concept of 'assumption of responsibility'. Summarising the judgment, Arden LJ stated:

*'in appropriate circumstances the law may impose on a parent company responsibility for the health and safety of its subsidiary's employees. ...*  
*(1) the businesses of the parent and subsidiary are in a relevant respect the same;*  
*(2) the parent has, or ought to have, superior knowledge on some relevant aspect of health and safety in the particular industry;*

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<sup>37</sup> See, eg, Halina Ward, 'Towards a New Convention on Corporate Accountability? Some Lessons from the Thor Chemicals and Cape PLC Cases' [2001] Yearbook of International Environmental Law 105; Carola Glinski, *Die rechtliche Bedeutung der privaten Regulierung globaler Produktionsstandards* (Nomos 2010) 332ff; ead., 'Corporate Self-Regulation: Moral or Legal Obligation?' in Doreen McBarnet, Aurora Voiculescu and Tom Campbell (eds), *The New Corporate Accountability: Corporate Social Responsibility and the Law* (Cambridge University Press 2007) 119.

<sup>38</sup> [2012] EWCA Civ 525. For detailed analysis, see Martin Petrin, 'Assumption of Responsibility in Corporate Groups: *Chandler v Cape plc*' (2013) 76 MLR 589, 603ff.; Siel Demeyere, 'Liability of a Mother Company for its Subsidiary in French, Belgian, and English Law' [2015] European Review of Private Law 385, 402ff.

(3) the subsidiary's system of work is unsafe as the parent company knew, or ought to have known; and

(4) the parent knew or ought to have foreseen that the subsidiary or its employees would rely on its using that superior knowledge for the employees' protection.

For the purposes of (4) it is not necessary to show that the parent is in the practice of intervening in the health and safety policies of the subsidiary. The court will look at the relationship between the companies more widely. The court may find that element (4) is established where the parent has a practice of intervening in the trading operations of the subsidiary, for example production and funding issues.<sup>39</sup>

In the aftermath of *Chandler v Cape*, courts in England but also in the Netherlands have seen an influx of cases relating to transnational corporations and their operations in developing countries. Royal Dutch Shell is facing litigation regarding the operations of its Nigerian subsidiary SPDC in the Netherlands<sup>40</sup> as well as in England.<sup>41</sup> The English company Vedanta is being sued in England, together with its Zambian subsidiary KCM, in relation to environmental damage caused by the copper mine that is operated by KCM.<sup>42</sup> Germany has not seen a transnational case dealing with human rights violations of corporations in recent years,<sup>43</sup> although in a recent empirical study, German corporations ranked number 5 among the countries whose companies most frequently received reports on human rights infringements abroad, after US American, British, Canadian and Chinese corporations.<sup>44</sup>

All these cases are still pending at the time of writing, at different stages, and a variety of issues, or barriers to the claims of victims, are subjects of controversial debates, amongst them prominently jurisdiction, the applicable law, and most crucially, substantive law.

Jurisdiction of EU Member States' courts for claims against parent companies that are domiciled in the relevant Member State is not normally a problem any longer, as under Article 4(1) of the Brussels Ia Regulation

<sup>39</sup> *Chandler v Cape plc* [2012] EWCA Civ 525 [80].

<sup>40</sup> See, eg, District Court of the Hague, 30/1/2013, *Fidelis Ayoro Oguru et al. v Royal Dutch Shell plc et al.*, <<https://milieudefensie.nl/publicaties/bezwaren-uitspraken/final-judgment-oguru-vs-shell-oil-spill-goi>> accessed 14 June 2017. See also Liesbeth Enneking, 'The Future of Foreign Direct Liability? Exploring the International Relevance of the *Dutch Shell Nigeria* Case' (2014) 10 *Utrecht Law Review* 44; Nicola MCP Jägers and Marie-Jose van der Heijden, 'Corporate Human Rights Violations: The Feasibility of Civil Recourse in the Netherlands' (2008) 33 *Brooklyn Journal of International Law* 833.

<sup>41</sup> See *Okpabi v Royal Dutch Shell Plc* [2017] EWHC 89 (TCC).

<sup>42</sup> See *Lungowe and others v (1) Vedanta Resources plc (2) Konkola Copper Mines plc* [2016] EWHC 292 (TCC).

<sup>43</sup> See Miriam Saage-Maaß and Maren Leifker, 'Haftungsrisiken deutscher Unternehmen und ihres Managements für Menschenrechtsverletzungen im Ausland' [2015] *Betriebs-Berater* 2499, 2501.

<sup>44</sup> See Kamminga, *supra* note 28, at 101 f.

(EU) No. 1215/2012,<sup>45</sup> defendants can be sued in the courts of the Member States where they are domiciled. In the case of *Owusu*,<sup>46</sup> the Anglo-Saxon doctrine of *forum non conveniens*, under which courts had been allowed to deny and had denied jurisdiction for reasons such as the impracticality of collecting evidence, political economy,<sup>47</sup> or even the workload of courts,<sup>48</sup> was rejected by the European Court of Justice (ECJ) as being non-compliant with the provisions of EU law, namely, the Brussels I Regulation (EC) No. 44/2001,<sup>49</sup> the predecessor of Regulation (EU) No. 1215/2012. English courts have accepted that decision ever since,<sup>50</sup> and current controversies concerning jurisdiction do not relate to the parent company but to the question whether or not the foreign subsidiary, who is *not* domiciled in an EU Member State, can nevertheless be sued together with the parent company, due to the connection between the claims, although the EU Member States' courts would clearly not have jurisdiction for these claims as, even in a multinational corporation, the individual legally independent companies have to be treated separately.<sup>51</sup> A connection of the claims has been accepted by the Dutch first instance court in *Oguru v Shell*,<sup>52</sup> and by the English High Court in the *Vedanta* case,<sup>53</sup> whereas it has been rejected in the *Okpabi* case where the first instance judge held that he saw no prospect of the claim against the parent company,<sup>54</sup> which would be a necessary precondition for the connection with the claim against the subsidiary.

The applicable law is to be determined in accordance with the provisions of the Rome II Regulation (EC) No. 864/2007.<sup>55</sup> Under Article 4(1), the law applicable to a non-contractual obligation arising out of a tort/delict shall be the law of the country in which the damage occurs irrespective of the country in which the event giving rise to the damage occurred and irrespective of the country or countries in which the indirect consequences of that event occur. In essence, this means that it is normally

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<sup>45</sup> OJ 2012 L 351/1.

<sup>46</sup> Case C-281/02 *Andrew Owusu v N.B. Jackson and others*, ECLI:EU:C:2005:120.

<sup>47</sup> See *In Re Union Carbide Corporation Gas Plant Disaster at Bhopal, India*, 1984, 634 F Supp. 842 (SD NY 1986).

<sup>48</sup> See *Rockware Glass v MacShannon* [1978] AC 795.

<sup>49</sup> OJ 2001 L 12/1.

<sup>50</sup> See, eg, the overview of cases in *Okpabi*, *supra* note 41, [67].

<sup>51</sup> See Gerhard Wagner, 'Haftung für Menschenrechtsverletzungen' (2016) 80 *Rabels Zeitschrift für ausländisches und internationales Privatrecht* 717, 733.

<sup>52</sup> See District Court of 's-Gravenhage, 30.12.2009, *Fidelis Ayoro Oguru et al. v Royal Dutch Shell plc et al*, ECLI:NL:RBSGR:2009:BK8616, <<http://deeplink.rechtspraak.nl/uitspraak?id=ECLI:NL:RBSGR:2009:BK8616>> accessed 14 June 2017.

<sup>53</sup> See *Vedanta*, *supra* note 42, [168].

<sup>54</sup> On which see *infra*.

<sup>55</sup> Regulation (EC) No. 864/2007 on the law applicable to non-contractual obligations, OJ 2007 L 199/40.

the law of the developing country where the subsidiary operates and where the victims suffered damage that applies. In many instances, the tort law systems of these countries belong to the common law world; which triggers the interesting question of whether or not the recent development of English common law with the case of *Chandler v Cape* applies. In *Oguru v Shell*, the District Court of the Hague regarded *Chandler v Cape plc* to be a part of Nigerian law.<sup>56</sup> English courts have been less bold until now, and in *Vedanta* as well as in *Okpabi*, the first instance judges heard experts from the relevant countries about their views of the application of *Chandler v Cape* in *Zambian* and *Nigerian* law respectively. Unsurprisingly, expert evidence supplied by the claimant and by the defendant differed, and the judges have not reached a conclusion yet on which opinion to follow.<sup>57</sup> Therefore, the following considerations first of all depend on the application of the *Chandler v Cape* criteria as part of the laws of the countries where the subsidiaries operate; which shall be assumed hereinafter.

In substantive law, one important distinction relates to the claimants: In the Dutch *Shell* cases as well as in *Vedanta* and in *Okpabi*, the claimants are not employees of the subsidiaries, as in *Chandler v Cape*, but neighbours that have been harmed by the pollution of the environment through oil and mining operations. Until now, courts have not entirely excluded the application of *Chandler v Cape* to this type of claimants. The first instance judge in *Vedanta* said this: 'For obvious reasons, such a claim is more likely to succeed if advanced by former employees ... However, depending on the facts, claims made by residents, rather than former employees, are still arguable.'<sup>58</sup>

Another problem of fact is the comparability of the corporate structures at issue. As mentioned above, under the second *Chandler v Cape* criterion, the parent has, or ought to have, superior knowledge on some relevant aspect of health and safety in the particular industry. In contrast, in the case of *Thompson v Renwick*,<sup>59</sup> liability of the parent company was denied because the parent company merely held shares in the subsidiary and did not possess superior knowledge in the field of business that the subsidiary was in. Thus, potential liability of the parent company heavily depends on the relationship between the parent company and the subsidiary. For example, the first instance judge in *Okpabi* argued that Royal Dutch Shell did not have any operations in Nigeria or anywhere; that it did not have any infrastructure in Nigeria; and that there was simply no evidence of a high level of oversight or high degree of control and direction, or indeed of any appreciable level of oversight or control either.

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<sup>56</sup> See *Oguru*, *supra* note 40, [4.30] and [4.34ff]. The Appeal Court of the Hague has not decided on that issue yet.

<sup>57</sup> See *Okpabi*, *supra* note 41, [58] f.; *Vedanta*, *supra* note 42, [123].

<sup>58</sup> See *Vedanta*, *supra* note 42, [115].

<sup>59</sup> [2014] EWCA Civ 635.

Thus, he could not see the *Chandler v Cape* criteria satisfied.<sup>60</sup> In contrast, the first instance judge in *Vedanta* saw a realistic chance to find that Vedanta has taken significant control over the operations of its subsidiary KCM.<sup>61</sup>

Following *Chandler v Cape*, a scholarly debate has also started in Germany, where authors discuss a potential duty to organise the corporation including its subsidiaries in such a manner that employees and other third parties do not suffer harm. That debate is by and large fictitious, as far as activities of German parent companies in developing countries are concerned, as German law will not apply to torts that cause damage in the host states<sup>62</sup> (although some authors try to bring German law to application, for example, as 'rules of safety and conduct' in the terms of Article 17 of the Rome II Regulation<sup>63</sup> or through the *ordre public* rule of Article 26 of the Rome II Regulation, in particular if otherwise the law of an unjust state applied).<sup>64</sup> A number of authors have argued towards an extension of the duty to organise the enterprise (*Betriebsorganisationspflicht*) to a duty to organise the corporation (*Konzernorganisationspflicht*).<sup>65</sup> Generally speaking, German authors are cautious but recognise a general development towards greater responsibility for the activities of subsidiaries.<sup>66</sup>

#### 2.1.2. SUPPLY CHAIN LIABILITY

The idea of supply chain liability is even more recent than the idea of the parent company's liability for its impact on the performance of subsidiaries. It has also been fuelled by the case of *Chandler v Cape*. In fact, the court in *Chandler v Cape* did not refer in any way to ownership of the parent company in the subsidiary but rather to dependence and control. In the aftermath, academic authors have argued that a comparable 'relationship of control', 'prior conduct that creates a situation of peril', 'superior knowledge' and a situation in which the 'injured party relies on

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<sup>60</sup> See *Okpabi*, *supra* note 41, [99].

<sup>61</sup> See *Vedanta*, *supra* note 42, [121].

<sup>62</sup> See also Wagner, *supra* note 51, at 739ff.

<sup>63</sup> See Saage-Maaß and Leifker, *supra* note 43, at 2502.

<sup>64</sup> See Axel Halfmeier, 'Menschenrechte und Internationales Privatrecht im Kontext der Globalisierung' (2004) 68 *Rabels Zeitschrift für ausländisches und internationales Privatrecht* 653, 671ff.; Marc-Philippe Weller, Luca Kaller and Alix Schulz, 'Haftung deutscher Unternehmen für Menschenrechtsverletzungen im Ausland' (2016) 216 *Archiv für die civilistische Praxis* 387, 394ff., for serious human rights violations.

<sup>65</sup> See, eg, Glinski, *supra* note 37, at 343ff.; Saage-Maaß and Leifker, *supra* note 43, at 2502ff.

<sup>66</sup> See, eg, Wagner, *supra* note 51, at 767; Weller, Kaller and Schulz, *supra* note 64, at 401ff.

the defendant' and his superior knowledge or resources may also exist in the relationship between suppliers and their purchasers.<sup>67</sup>

Following spectacular disasters, in particular in the garment industry in Pakistan and Bangladesh, the first cases relating to supply chain responsibility have reached the courts. In Germany, four victims of the Ali Enterprises factory fire in Karachi have sued the garment discounter KiK, the main customer of Ali Enterprises, for damages.<sup>68</sup> Outside EU jurisdictions, victims of the Rana Plaza collapse in Bangladesh have initiated a class action in the US against several retailers,<sup>69</sup> and a similar law suit has been filed in Ontario.<sup>70</sup>

In terms of jurisdiction, no problems arise in EU Member States. In particular, victims would not normally try to sue the suppliers together with the purchasers as the suppliers lack relevant funds. In fact, if suppliers are large enough to be attractive defendants, the level of control of the purchaser over the supplier is likely to be insufficient to justify supply chain liability.

The applicable law is again the law of the country where the damage occurred. Thus, in the German KiK case, the applicable law is the law of Pakistan,<sup>71</sup> and therefore, again, *Chandler v Cape* may be relevant, as the LG Dortmund may find that case to be part of Pakistani law. In *Rahaman*, the Superior Court of Delaware applied Bangladeshi law to the issue of prescription but not to the employer's liability claim.<sup>72</sup>

In terms of substantive law, courts would need to be prepared to apply the *Chandler v Cape* criteria to supply chains, as proposed above. In *Rahaman*, the Superior Court of Delaware applied the general rules (of the law of Delaware) regarding an employer's liability for the employees of an independent contractor without mentioning *Chandler v Cape* at all; which also the claimants apparently have not pleaded. The action was dismissed.

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<sup>67</sup> See Peter Rott and Vibe Ulfbeck, 'Supply Chain Liability of Multilateral Corporations?' [2015] *European Review of Private Law* 415. See also Andrew Sanger, 'Crossing the Corporate Veil: The Duty of Care Owed by a Parent Company to the Employees of its Subsidiary' (2012) 7 *CLJ* 478, 480; Cees van Dam, 'Tort Law and Human Rights: Brothers in Arms' (2011) 2 *Journal of European Tort Law* 221, 251; Demeyere, *supra* note 38, at 390.

<sup>68</sup> LG Dortmund, 7 O 95/15. For details, see Philipp Wesche and Miriam Saage-Maaß, 'Holding Companies Liable for Human Rights Abuses Related to Foreign Subsidiaries and Suppliers before German Civil Courts: Lessons from *Jabir and Others v KiK*' (2016) 16 *Human Rights Law Review* 370, 372ff.

<sup>69</sup> Delaware Superior Court, *Abdur Rahaman et al. v JCPenney Corp. Inc. et al.*, C.A. No. N15C-07-174 MMJ.

<sup>70</sup> *Das v George Weston Limited*, No. CV-15-526628 (Ont. Superior Ct. filed Apr. 22, 2015).

<sup>71</sup> LG Dortmund, press statement of 30/8/2016, <[www.lg-dortmund.nrw.de/behoerde/presse/Pressemitteilungen/PM-KiK\\_docx.pdf](http://www.lg-dortmund.nrw.de/behoerde/presse/Pressemitteilungen/PM-KiK_docx.pdf)> accessed 14 June 2017.

<sup>72</sup> See *Rahaman*, *supra* note 69.



German scholars are also discussing supply chain liability under German tort law, and reluctance is even greater than with regard to organisational duties in corporate structures.<sup>73</sup>

## 2.2. IMPACT ON DIRECTORS' DUTIES?

As explained above, the duty to avoid unnecessary liability risks requires consideration of the extension of the risk and the likelihood of its materialisation. Looking at the degree of damage caused by subsidiaries in developing countries and the number of people affected, the extension of the risk is significant. For example, in *Bodo Communities*, the Shell Petroleum Development Company of Nigeria paid £55 million in settlement.<sup>74</sup> In *Okapbi and others v RDS and SPDC*, the claimant chiefs of the Ogoni people represent around 42,000 people. The *Vedanta* law suit concerns 1,826 claimants. In the *KiK* case, four test claimants claim €30,000 each. Shortly after the admission of the claim and the grant of legal aid, KiK agreed to pay US-\$5.15 Mio. to the victims.<sup>75</sup> The Rana Plaza factory collapse, which was subject to the *Rahaman* litigation, claimed 1,130 deaths and injured 2,500. In the *Das* case pending in Ontario \$2 billion are at stake.<sup>76</sup> Law firms have sent messages to their transnational corporations clients warning them against the new liability risks.<sup>77</sup>

The likelihood of the materialisation of the risk, in contrast, is difficult to estimate as all the law suits are still pending, and until now, almost no parent company has been successfully sued; in the case of *Bodo Communities*, it was the subsidiary SPDC who paid £55 million in settlement. Academic authors are also divided about the prospects of the claims as well as about the desirability of any duties of parent companies related to the activities of subsidiaries in developing countries. Thus, it is clearly not possible to argue that passivity on part of the parent company concerning the subsidiaries' operations *will* lead to tort law liability, whereas it *might* lead to tort law liability.

The same applies to supply chain liability where, intuitively, the idea of liability arising from supply chain control appears to be even more remote. Litigation is still at an early stage, and the best one can say at this

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<sup>73</sup> See, eg, Wagner, *supra* note 51, at 771ff.

<sup>74</sup> *The Bodo Community and Others v The Shell Petroleum Development Company of Nigeria Ltd* [2014] EWHC 1973 (TCC).

<sup>75</sup> See ECCHR, 'Der Preis der Katastrophen in der Textilindustrie Südasien', <[www.ecchr.eu/de/unsere-themen/wirtschaft-und-menschenrechte/arbeitsbedingungen-in-suedasien/pakistan-kik.html](http://www.ecchr.eu/de/unsere-themen/wirtschaft-und-menschenrechte/arbeitsbedingungen-in-suedasien/pakistan-kik.html)> accessed 14 June 2017.

<sup>76</sup> See Michelle Chen, 'A Western Company Could Finally be Held Accountable for the Rana Plaza Disaster' (*The Nation*, 29 April 2016) <[www.thenation.com/article/a-western-company-could-finally-be-held-accountable-for-the-rana-plaza-disaster](http://www.thenation.com/article/a-western-company-could-finally-be-held-accountable-for-the-rana-plaza-disaster)> accessed 14 June 2017.

<sup>77</sup> See Birgit Spießhofer, 'Wirtschaft und Menschenrechte – rechtliche Aspekte der Corporate Social Responsibility' [2014] NJW 2473.

time is that the claims of subsidiaries' employees have not been struck out immediately, and that legal aid has been granted in Germany; which means that the court does not deny the possibility of a successful claim (predominantly due to lack of knowledge of the law of Pakistan). Application of *Chandler v Cape* to supply chains has not been tested in the failed *Rahaman* litigation in Delaware.

### 2.3. LIMITATIONS

Tort law of course has its own limitations in that it usually requires physical damage, whereas liability for non-pecuniary damage is by and large excluded. Thus, tort law may impose liability on transnational corporations where insufficient health and safety precautions and environmental protection lead to physical damage and consequential loss of employees and neighbours, or where there is responsibility for human rights violations committed by security personnel in the neighbourhood. In contrast, it would seem impossible to catch other CSR issues such as, in particular, minimal wages, excessive working hours (unless they lead to health problems), or obstruction of workers' associations.

## 3. LEGAL UNCERTAINTY

Of course, the law is not always clear. Legal uncertainty is a problem that arises both with regard to the duty to avoid unnecessary risks and with the legality principle. In principle, these situations need to be distinguished, as the appreciation of business risks, including liability risks, come under the business judgment rule whereas the legislator has made it clear that the business judgment rule does not apply to compliance with legal obligations under the legality principle. Nevertheless, it has been argued in academic writing that the criteria that are to be applied to the business judgment rule may also apply in situations of legal uncertainty, as in such situations, there will also be some margin of appreciation.<sup>78</sup>

How do directors deal with this legal uncertainty? Clearly, directors will have to investigate the legal situation.<sup>79</sup> This will normally require them to seek professional advice,<sup>80</sup> in particular when it comes to the application of foreign law.<sup>81</sup> Whether or not asking the internal legal department of the company suffices depends on the circumstances, such as the time that is available for the decision, but also the risk. Here, it should be recalled, that in CSR matters such as health and safety and environmental degradation the extension of the risk might be quite significant. The courts lean towards a duty to seek external advice,<sup>82</sup> and even then, directors should be wary that in long-term relationship with an external,

<sup>78</sup> See Spindler, *supra* note 2, margin note 75; Kocher, *supra* note 35, at 217.

<sup>79</sup> See Spindler, *supra* note 2, margin note 77.

<sup>80</sup> See BGH *Neue Zeitschrift für Gesellschaftsrecht* 2011, 1271.

<sup>81</sup> See Kocher, *supra* note 35, at 220.

<sup>82</sup> See OLG Stuttgart, *Neue Zeitschrift für Gesellschaftsrecht* 2010, 141.

independence may suffer over time.<sup>83</sup> Quite obviously, the external professional must possess the relevant expertise,<sup>84</sup> or his or her selection may trigger director's liability.<sup>85</sup>

If the director can derive from professional advice that the courts may interpret the law in favour of the company, he does not act in breach of his duty if he acts on the basis of such favourable interpretation.<sup>86</sup> This would mean that in the current situation of legal uncertainty about a transnational corporation's liability for damage that occurs in the country where the subsidiary or the supplier operates, the director would not be under the general *duty* to do everything to avoid that damage to occur; although it would seem that, again, the closer the situation to the *Chandler v Cape* criteria, and therefore, the greater the risk of liability, the more likely it is for a court to find a breach of duty.

At the same time, there should be no doubt that the recently increased risk of liability in corporate structures and even in supply chain situations give directors the *right* to integrate risk avoidance measures in their decisions. Certainly, they have to follow the legal development, in particular the pending litigation, closely.<sup>87</sup>

#### 4. CONCLUSION

Pursuing corporate social responsibility goals as such is surely not a duty of directors under German law. The directors' duties under the legality principle only apply to existing legal obligations or to self-commitments of a company, through its competent bodies, to CSR soft law or private regulation. Directors, however, also have to avoid unnecessary risks, under the business judgment rules. Here, the increasing risk of tort liability in the aftermath of *Chandler v Cape*, with the influx of cases in several jurisdictions, may lead to the duty but surely to the right of directors to organise the transnational corporation or the supply chain in such a way that damage is avoided, even if this is more costly than the often ruthless business policy of the past.

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<sup>83</sup> See Spindler, *supra* note 2, margin notes 78 and 80.

<sup>84</sup> See OLG Stuttgart, *Neue Zeitschrift für Gesellschaftsrecht* 2010, 141.

<sup>85</sup> For an overview, see Holger Fleischer, 'Vorstandshaftung und Vertrauen auf anwaltlichen Rat' [2010] *Neue Zeitschrift für Gesellschaftsrecht* 121.

<sup>86</sup> See Spindler, *supra* note 2, margin note 83.

<sup>87</sup> See also Liisa-Julia Voß, 'Saage-Maaß, Miriam/Leifker, Maren – Haftungsrisiken deutscher Unternehmen und ihres Managements für Menschenrechtsverletzungen im Ausland, in: *BB* 2015, S. 2499 – 2504' [2015] *Newsdienst Compliance* 42101.