



MODERN SLAVERY & THE HOTEL INDUSTRY

Best Practice Guidance for Franchising

Archana Kotecha, Liberty Shared

James Hargrove, Orrick

LIBERTY SHARED

CREATING AN ENVIRONMENT
SAFE FROM TRAFFICKING


orrick

AUTHORS

Archana Kotecha is the Asia Region Director and Head of Legal for Liberty Shared, based in Hong Kong. Archana has extensive experience in the areas of advocacy, policy work and casework relating to trafficking in persons. Archana has published many reports and best practices and advised governments, financial institutions, regulators and corporates on human trafficking including legal and anti-money laundering frameworks and human rights risks.

James Hargrove is an Orrick partner specializing arbitration and litigation, based in Geneva and London. James has also worked for the Liberty human rights organization and Human Rights Watch in London. James has published articles and advises corporate and pro bono clients on business and human rights issues.



In response to growing awareness and legislation, many companies have adopted policies in an attempt to eradicate Modern Slavery. Certain industries, however, remain “hot-spots” for human rights abuses, such as the hotel industry, and in particular hotels operating under major international brand franchises. This guide provides franchisors with an overview of the risks associated with Modern Slavery in relation to hotel franchise agreements and sets out practical solutions to aimed at increasing the prospect that a franchisee’s operations are free from these risks.¹

¹ Note. You have asked us to prepare a guide setting out the risks hotel industry franchisors face in relation to Modern Slavery and the steps franchisors can take to tackle and prevent this risk. Because franchise liability law and laws relating to Modern Slavery vary from jurisdiction to jurisdiction, this guide only provides a high-level analysis of the current issues arising in this area of the law. This guide is not intended to replace jurisdiction-specific research regarding the liability of franchisors and franchisees for acts constituting Modern Slavery. Should Liberty Shared require further research regarding a specific jurisdiction, Orrick would be happy to provide such additional information.

What is Modern Slavery?

Modern Slavery is the use of force, fraud or coercion to compel a person to provide labour, services or sexual acts against his or her will. It encompasses slavery and servitude, forced or compulsory labour and human trafficking (collectively, "Modern Slavery").

Modern Slavery taints many industries around the world. The United Nations Office on Drugs and Crime ("UNODC") has stated that virtually no country is immune from it, and its victims are men, women and children of all ages and backgrounds. It is difficult to establish how many victims there are because of issues with detection and under-reporting. The International Labour Organisation ("ILO") estimates there are over 40.3 million people trapped in Modern Slavery globally.² Out of



the 24.9 million people trapped in forced labour, the ILO estimates that 16 million are exploited in the private sector such as domestic work, construction or agriculture, 4.8 million in forced sexual exploitation, and 4 million in forced labour imposed by state authorities. The ILO estimates that women and girls are disproportionately affected by forced labour, accounting for 99% of victims in the commercial sex industry, and 58% in other sectors. According to the ILO, the most prevalent regions for Modern Slavery are Asia and the Pacific and Africa. The UNODC describes Modern Slavery as one of the fastest growing criminal enterprises in the World, third after drug dealing and the arms trade, with estimated annual global profits of USD 150 billion. Criminal organisations are switching to human slavery due to higher profits and lower risk of detection. It is one of the great criminal threats of our time, and it infects many of the industries that we use in our daily lives.

The acknowledgement of modern slavery as part of the global development agenda, the Sustainable Development Goals ("SDG"), is a move that is indicative of the serious risk that modern slavery has posed and continues to pose to the global community. The rise of transparency in supply chain regulations also raises the stakes for companies that operate global supply chains and elevates the responsibility to identify, manage and mitigate these risks.

The Current Legal Framework

In recent years, there has been an increase in international legal instruments and legislation aimed at combatting Modern Slavery and associated abuses. These can be separated into two groups:

Advisory Documents

Presently, there are the so-called "soft law" advisory documents, setting out ethical norms and proposed best practices, which are not of mandatory legal application and carry no legal sanction for breach. The most commonly cited example is the United Nations Guiding Principles on Business and Human Rights (the "Guiding Principles"). The Guiding Principles comprise 31 different principles setting out a global standard for protecting against human rights abuses in international business activities, the implementation of which is regularly reviewed by the United Nations Human Rights Council's ("UNHRC") working group. The Guiding Principles are divided into three main pillars of responsibilities and / or obligations which should be implemented by compliant states and businesses, as follows:

- State protection of human rights;
- Corporate responsibility to respect human rights; and
- Provision of legal remedies for victims of human rights abuse in business.

² ILO, "Global Estimates of Modern Slavery", available at https://www.ilo.org/wcmsp5/groups/public/@dgreports/@dcomm/documents/publication/wcms_575479.pdf

National Legal Instruments

Already existing national legal instruments are of mandatory application and ultimately can be enforced by the courts of that jurisdiction. These instruments can carry legal sanctions for certain breaches. Examples of such laws, without limitation, include the UK Modern Slavery Act (2015) ("MSA"), the Italian Legislative Decree 231/2001 ("231 Decree"), the French Law n° 2017-399 ("L. n° 2017-399") and the California Transparency in Supply Chains Act (2010) ("TSCA"), all of which apply to companies operating within the UK, Italy, France and California respectively, regardless of place of incorporation, as follows:³

- The MSA is applicable to all companies carrying out business in the UK having a global annual turnover of at least GBP 36 million. It consolidates English law on slavery and trafficking offences, for which individuals and companies may be criminally liable, and creates new defences and remedies for slavery and trafficking victims compelled to commit crimes. An Anti-Slavery commissioner's office was also created to monitor and prevent Modern Slavery offences. The MSA requires that all applicable companies annually disclose steps taken to ensure Modern Slavery does not occur in that company's supply chain or declare that no steps have been taken. Failure to do so may result in an unlimited fine following injunctive relief sought by the Home Secretary;

- The 231 Decree is applicable to all companies carrying out business in Italy. Pursuant to the 231 Decree, sanctions are imposed on companies for particular crimes committed in their interest or advantage by their managers and employees. The liability provided for in the 231 Decree - which is in addition to that of the individual - applies in relation to the commission of numerous crimes including slavery, forced labour and human trafficking;
- France's law on the "duty of vigilance for parent and instructing companies", L. n° 2017-399, is aimed at France's largest companies, applying to any company incorporated in France that has for two consecutive years employed at least 5,000 employees and whose head office is located in France or employs 10,000 employees within the company and its direct and indirect subsidiaries, whose head office is located on French territory or abroad. The duty of vigilance imposes three obligations: (i) to implement a vigilance plan to identify risks and prevent human rights abuses that may result from the activities of the company, or the companies it

³ Proposals for Modern Slavery legislation are pending in Australia (i.e., the Modern Slavery Bill 2018), and the Netherlands (i.e., Wet Zorgplicht Kinderarbeid (the "Child Labour Due Diligence Law"). In Switzerland, the Legal Affairs Committee of the Swiss National Council put forward an indirect counter-proposal in response to the "Responsible Business Initiative." On June 14, 2018, the counter-proposal was approved by the Swiss National Council and awaits further determination. In Germany, the National Action Plan establishes a set of clear expectations and goals concerning the implementation of human rights due diligence by German companies. The voluntary code is due to be reviewed in 2020 to assess whether voluntary commitment sufficient or whether the implementation of legislation is necessary.



controls, or from the activities of any subcontractors or suppliers; (ii) to ensure effective implementation of the vigilance plan; and (iii) to publish a report concerning implementation to be included in the company's annual management report. Failure to comply with the law may attract periodic penalty payments and civil liability action; and

- The TSCA is applicable to any retail or manufacturing company of global annual turnover of more than USD 100 million, which is liable for tax and doing business in California. Like the MSA, it requires all such companies to make written disclosures on efforts to prevent trafficking and slavery within their respective supply chains and unlimited fines may be imposed if a company fails to comply with these requirements following a successful action for injunctive relief by the State Attorney General.

In the future, there is a real possibility that there will be binding international legislation, with sanctions for breaches. This discussion is continuing, for example, in the UNHRC's "Open-Ended Intergovernmental Working Group on Transnational

Corporations and other Business Enterprises with Respect to Human Rights", which met in October 2018 for a fourth session to discuss the draft of a binding international treaty. Although several more meetings will be required to consider and potentially amend the draft treaty, it is likely that sufficient international support exists to ratify and implement an eventual treaty within the next three years. More than 100 states and 200 civil society organizations have participated in the drafting process to date.

In summary, there already exists binding legislation, and widely accepted soft law principles applying to Modern Slavery. International legislation is currently being drafted. Therefore, all national and international businesses who might be affected ought to take legal advice to understand their obligations and measure their related risks.

Business obligations in relation to human rights issues, including the issue of Modern Slavery, present a serious legal, regulatory and reputational risk and are therefore now at the forefront of boardroom strategy, especially in the hotel industry.

⁴ Combat Human Trafficking available at <https://www.brookes.ac.uk/about-brookes/news/combatact-project-aims-to-tackle-hotel-industry-s-role-in-human-trafficking/>.

Modern Slavery in the Hotel Industry

As a major global business sector employing millions of people, including in many regions where the rule of law is weak and Modern Slavery prevalent, the hotel industry faces substantial risks in relation to Modern Slavery. There are three clear areas where Modern Slavery can occur:

- Hotels can unknowingly be used to exploit victims, particularly victims of sexual exploitation who may be moved through the hotel when being trafficked, or kept in the hotel by traffickers who use hotel bedrooms as a base for sexual exploitation;
- Workers recruited or subcontracted via unscrupulous agencies (often in lower skilled roles such as housekeeping) may be the victims of forced labour and debt bondage (e.g., forced to work, extortionate recruitment fees charged leading to indebtedness, and passports / identity documentation confiscated); and
- A hotel's supply chain such as products passing through a complex network of producers, distributors, and vendors before being brought into hotels, may also carry the risk that they are tainted by exploitation.

It is estimated that, annually, there are over 1.1 million victims of Modern Slavery in Europe, including over 93,000 sex slaves and 4,500 victims of forced labour exploited in hotels.⁴

Issues in Franchise Arrangements

The hotel industry is inherently vulnerable to Modern Slavery due to the nature of the industry, the web of commercial relationships connected with each hotel and the consequent needs of each hotel, such as the need for a wide array of reasonably priced services, its seasonality and labour supply.

Within this context, the franchise system is particularly exposed to risks in relation to Modern Slavery, since:

- The franchisee will adopt and get the benefit of the franchisor's brand, but may not share or implement its ethical standards and practices;
- Often the franchisees will be in regions where the rule of law is weak and / or the cultural approach to Modern Slavery does not accord with the norms where the franchisor is based;
- A franchise agreement, for reasons explained in the section headed "What Level of Control can Franchisors Exert Over Franchisees" below, does not usually provide the franchisor with the right to ensure the franchisee's operations are in compliance with its ethical standards and practices, both in relation to labour supply, and the supply of goods services to the hotel; and
- It is difficult for the franchisor to be assured that companies in the hotel's supply chain do not commit acts of Modern Slavery, such as agencies supplying labour.

It is important that franchisors are aware of these risks, and are informed about how to address them, all with the ultimate aim of promoting best practices, respect for human rights, a zero-tolerance of human slavery,

and a better future for millions of exposed persons associated with the hotel industry. In the section headed "Potential Practical Steps for Franchisors" below, we have provided a practical guide to steps franchisors can take.

⁵ See, e.g., *Sinaltrainal v. Coca-Cola Co.*, 256 F. Supp. 2d 1345, 1354 (S.D. Fla. 2003), *aff'd*, 578 F.3d 1252 (11th Cir. 2009). The court in *Sinaltrainal* examined the franchise agreement and held that Coca-Cola "did not have a duty to monitor, enforce, or control labor policies at a bottling plant" operated by franchisees and the agreement did not impose any duty related to labour practices, therefore Coca Cola had therefore not acted jointly with the bottler in the violation of international law); see also *McFarland v. Breads Of The World*, Case No. 1:09-cv-929, 2011 WL 801815, at ** 8-12 (S.D. Ohio Feb. 1, 2011) (franchisor does not proscribe and/or enforce employment policies on behalf of its franchisees, it will therefore not be deemed the employer and thus it is not vicariously liable for the actions of the franchisees), *report and recommendation adopted by*, 2011 WL 801793 (S.D. Ohio Mar. 2, 2011); see also *Courtland v. GCEP-Surprise, LLC*, Case No. CV-12-00349, 2013 WL 3894981, at *7 (D. Az. July 29, 2013) ("vicarious liability attaches for employment discrimination if the franchisor exerts daily control over the hiring, firing, and supervision of franchisee employees"); see also *Patterson v. Domino's Pizza, LLC*, 60 Cal.4th 474, 498 (Aug. 28, 2014) ("A franchisor ... becomes potentially liable for actions of the franchisee's employees, only if it has retained or assumed a general right of control over factors such as hiring, direction, supervision, discipline, discharge, and relevant day-to-day aspects of the workplace behaviour of the franchisee's employees. Any other guiding principle would disrupt the franchise relationship.") In England, there is little case law on this issue, however, the courts have described the relationship as more akin to a vendor/purchaser requiring independence and an arm's length approach suggesting that control exerted by a franchisor in a franchisee's operations would transform the relationship and the franchisor's liability in relation to the acts of the franchisee. See *Office Overload Ltd v Gunn* [1977] FSR 3; *PSG Franchising Limited v Darby & Others* [2012] EWHC 3707 (QB) citing *Dyno-Rod Plc v Reeve* [1998] FSR 148 at 153; *Fleet Mobile Tyres Ltd v Stone and another* [2006] EWCA Civ 1209.

⁶ See footnote 5 above.

⁷ McDonald's Corporate Social Responsibility & Sustainability Report 81 (2012-2013) available at https://corporate.mcdonalds.com/content/dam/gwscorp/scale-for-good/2012_2013_csr_report.pdf; Business & Human Rights Resource Centre, *McDonald's Company Action Plan Survey Response*, <http://business-humanrights.org/en/mcdonalds-0?issues%5B%5D=11245>

What Level of Control Can Franchisors Exert Over Franchisees?

A central issue for franchising across a number of jurisdictions is the allocation of legal and operational risk for human slavery abuses between franchisee and franchisor.⁵ In some jurisdictions, it is common for franchising agreements to contain provisions disclaiming any principal/agent relationship between the franchisor and franchisee and excluding liability for franchisee activities. It is common for such clauses to be effective, so long as the franchisor has not exerted “control” over the franchisee’s operations.

This is an important issue in the context of Modern Slavery because, as a broad generalisation, franchisors who impose *their own* ethical standards on franchisees may no longer be regarded as being in an arms-length commercial relationship, and may be held liable for the acts of franchisees (in the same way as an employer would be liable for the acts of an employee). However, it is important to note that

this issue is jurisdiction-specific. The law on this issue varies in different countries, and local counsel advice should always be taken. Franchisors will need to obtain legal advice from local counsel in each relevant jurisdiction to identify the specific legal risks to the franchisor from directing franchisees in relation to standards on Modern Slavery.

Subject to the above, it is true that franchisors often seek to shield themselves from liability for a franchisee’s violations of human rights, on the basis that the franchisor has not “controlled” the franchisee. This can be done by the franchisor, for example, suggesting, but not imposing, the franchisee’s adherence to the franchisor’s corporate social responsibility policy. For example, McDonald’s adopted a human rights policy in 2014, but with the caveat that it could not impose the policy on franchisees. McDonald’s confirms that “[m]ore than 80% of McDonald’s restaurants are owned and operated by independent Franchisees. The company expects its Franchisees to maintain high standards of integrity and to abide by all applicable laws and regulations, including laws regarding human rights, dignity and respect, workplace safety, and worker compensation and treatment. Ultimately, Franchisees define and implement people practices in their local restaurants.”⁷

However, there is of course a flip-side: if the franchisor seeks to strictly limit its relationship and not exercise control and supervision over the franchisee, there is a

greater risk that acts of Modern Slavery will occur, particularly if the hotel is located in an area where Modern Slavery is prevalent. This will, in any event, at least be *associated* with the franchisor / the brand (even if not legally liable for it), which will be prejudicial – the damage and fallout can be enormous.

The recent difficulties faced by the 7-Eleven business in Australia is an example of the damage that can be caused across a brand even where the franchisor was not legally liable for breaches by franchisees. In the context of allegations of widespread wage exploitation in Australia, representatives of 7-Eleven Australia, the franchisor, were called to testify before the Australian Senate adversely affecting the 7-Eleven brand and its profits. The Senate Inquiry Report entitled “*A National Disgrace: The Exploitation of Temporary Work Visa Holders*” recommended review of the Australian Franchising Code “with a view to assessing the respective responsibilities of franchisors and franchisees regarding compliance with workplace law and whether there is scope to impose some degree of responsibility on a franchisor and the merits or otherwise of so doing.”⁸ While this review is ongoing, Michael Smith, chairman of 7-Eleven Australia admits “*there’s no doubt the board should have known ...*”



⁸ The Australian Senate, *A National Disgrace: The Exploitation of Temporary Work Visa Holders*, Recommendation 26, para. 8.285 available at https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Education_and_Employment/temporary_work_visa/~/_media/Committees/eet_ctte/temporary_work_visa/report/report.pdf

⁹ Financial Review, *Can 7-Eleven chairman Michael Smith fix the company after wages scandal?*, 30 November 2017 available at <https://www.afr.com/brand/boss/how-chairman-michael-smith-is-saving-7eleven-20171102-gzdk75>

We should have been closer to the franchisees' businesses, including understanding the predominant cultures in our network, and running our own stores."⁹ The company subsequently entered into a compliance deed with the Fair Work Ombudsman, which included the introduction of centralised payroll, biometric clock on and off systems, and reporting procedures. Interestingly, the headquarters now runs over 60 stores.

The franchisor may, therefore, take the position that it wishes its contractual counterpart, the franchisee, to have human rights policies and procedures in place. In this regard, the franchisor needs to consider the extent it wishes to control the implementation and compliance of such policies; weighing the potential consequences of "control", the opportunity to set a framework for incremental and lasting change, and mitigate the risk of expensive and damaging fallout from franchisee abuses.

Of course, there is always a balancing to be carried out, taking into account the franchisor's position. We have set out below a list of potential practical steps.

Potential Practical Steps for Franchisors

If a franchisor has decided to take steps to impose a Modern Slavery review programme on franchisees, and/ or to monitor their activities, there are a range of steps it can take. As explained above, the franchisor will still have a decision to take as to how much control it wishes to exert over the franchisee. We have set out below some steps that franchisors may take towards limiting the likelihood of Modern Slavery abuses, but potentially without controlling the franchisee to such an extent that the franchisor risks being vicariously liable for infringements and also obtain protection from the franchisee by way of indemnity (again, this is jurisdiction-specific and advice should be taken from local counsel):

- Prior to entering into a franchise agreement, a franchisor should conduct jurisdiction-specific research regarding the liability of franchisors and franchisees for acts constituting Modern Slavery. This would require the franchisor to research, measure and consider the specific franchisee country risk, including the overall risk of abuse;
- Prior to entering into a franchise agreement, a franchisor ought to take legal advice on what mandatory legislation is applicable;
- Prior to entering into a franchise agreement, a franchisor ought to conduct targeted due diligence on the franchisee, including:
 - Reviewing any current anti-Modern Slavery policies in place, including whether the policies make provision for independent audit and inspections. If no such policies exist, a franchisor should consider carefully whether



to proceed with the franchise arrangement;

- Reviewing how such policies are communicated, implemented and monitored;
- Reviewing the labour practices of the potential franchisee, whether it uses agency staff, migrant workers, temporary labour and potentially obtaining information and further due diligence on agencies and recruitment fees payable by workers and assessment of passport-retention practices given that passport retention violates the law and is an indicator of forced labour although on its own it is not adequate to point to the existence of forced labour;
- Reviewing the supply chain practices of the potential franchisee and potentially obtaining information and further due diligence on supply chain companies; and
- Reviewing operational grievance mechanisms and requiring disclosure of all labour and human rights-related violations (also for agencies and supply chain companies);

- The franchisor may require that the franchise agreement contain indemnities from the franchisee and/ or liquidated damages provisions in relation to breaches by the franchisee of the above human rights practices, monitoring and enforcement procedures;
- On the basis that a potential franchisee has an anti-Modern Slavery policy in place, the franchise agreement may set out the franchisee's compliance with its policy and procedures. Additions to the franchise agreement may include:
 - Incorporation of the franchisee's pre-existing corporate social responsibility policy into the franchise agreement as an Annex;
 - Incorporation of the franchisee's pre-existing anti-Modern Slavery policy into the franchise agreement as an Annex;
 - Drafting into the franchise agreement a confirmation and undertaking that the franchisee warrants that it adopts and currently enforces social responsibility and anti-Modern Slavery policies, including in relation to its supply chain, which are compliant with national legislation and the Guiding Principles referred to above;
 - Drafting into the franchise agreement an undertaking that the franchisee warrants to maintain the above-described policies throughout the duration of the franchise agreement;
 - Drafting into the franchise agreement an undertaking that the franchisee warrants to disclose all detected incidents and remedial actions;
- Drafting into the franchise agreement that any breach of defined human rights-related obligations gives the right of the franchisor to terminate the agreement, with an indemnity or liquidated damages from the franchisee.

Once the appropriate jurisdiction-specific research is carried out, it should not be a complex process to include some or all of the above provisions in a franchise contract. The franchisor's corporate counsel should be able to advise on appropriate drafting.

The purpose of the above is for the franchisee to be required to take reasonable steps to incorporate and adhere to an anti-Modern Slavery policy, and prevent Modern Slavery, and promote accountability and transparency from and for all stakeholders.

Of equal importance is to keep up to date on the law. Modern Slavery is a global hot topic: further national legislation such as the new bills in Australia, Switzerland and the Netherlands are bound to be enacted and an international treaty is likely a matter of *when*, not *if*.

orrick.com

AMERICAS | EUROPE | AFRICA | ASIA

Orrick, Herrington & Sutcliffe LLP | 51 West 52nd Street | New York, NY 10019-6142 | United States | tel +1 212 506 5000
Attorney advertising. As required by New York law, we hereby advise you that prior results do not guarantee a similar outcome.

©2018 Orrick, Herrington & Sutcliffe LLP. All rights reserved.

