

Chapter Nine: Respect for Human Rights in Direct Customer Relationships

Overview

Overview of direct customer relationships

This chapter focuses on instances where a company has a direct relationship with the customer, end-user or consumer – referred to in this chapter as “direct customers”. Direct customers can be different types of actors including other businesses, governments and the individual consumer. Agreements with customers can be expressed in a variety of types of contractual relationships. A direct customer agreement is the means by which two or more parties enter into a legal relationship with regards to the possession or use of goods, property, and, in some cases, use of services. The most common type of contractual relationship with customers is a sales or service agreement (or a combined sales and service) agreement. These contracts can cover a wide range of exchanges, including the selling and purchasing of goods, real estate, personal property, securities and services. The laws governing the agreement will depend on the terms of the contract and national law. Contracts are generally voidable if they are entered into under duress, undue influence, fraud, or misrepresentation or if the contract violates public policy.

At times, a company will not have a direct interaction or contract with the consumer or end-user of a product or service that it sells. While the customer buying a product may conduct due diligence on the product and producer, it is less common, except in the case of large business-to-business purchases, for the seller to do due diligence on the customer. In the case of large purchases, where reputational issues associated with the product or potential legacy issues may exist, sellers may carry out due diligence on their customers. Where the end customer is a consumer, the seller’s options for undertaking due diligence may range from limited to impossible.

The conditions set out in sales contracts vary widely depending on what is for sale. They may be simple standard form contracts to very detailed sales contracts accompanied by extensive conditions of sale for larger products or services. Companies may specify and take action regarding how, by whom, in what circumstances and on what terms its products and services are consumed or used. Sellers may provide instructions or training to accompany their product to instruct customers on the appropriate use of products to limit misuse. In certain industries, there may be regulatory requirements or industry practice around including conditions on the final use and disposal of products. Servicing arrangements after sale provide an opportunity to assess the condition and use of goods sold or to provide on-going services.

Human rights and direct customers

There are a number of reasons why businesses may consider human rights impacts when engaging with direct customers, for example:

- As recent cases have shown, companies are being held responsible for acts of their customers, sometimes through legal proceedings. The increasingly wide range of

examples of product and service misuse may prompt further equally creative human rights due diligence around customer identity and use.

- Consumer-facing companies in particular sectors have been and continue to be under pressure from their consumers around their human rights performance – particularly in their value chain but also related to how consumers themselves might be impacted by products or services. As consumer focus on respecting human rights shifts to new industries, so too will those sectors have to increase their attention to human rights.
- Some products termed “dual use” are intended for benign purposes, but can be used for actions that violate human rights – this can cover a wide range of products and services from an equally wide range of sectors, from information and telecommunications to chemicals to pharmaceuticals and medical equipment, to financial services. As evidence of misuse comes into the public domain, companies will be under more pressure to understand and prevent potential misuse of their products or services.
- The human rights implications for customers of online purchasing, internet services and social networking has been a major topic in recent years. The concern relates to customer privacy and freedom of expression. The ways in which companies conduct due diligence, construct agreements and monitor their implementation for consumers and customers is attracting interest and scrutiny.

Orienting and Embedding – Internal Company Management of Direct Customer Relationships

Consumer expectations about human rights can focus a company’s attention.

Several respondents remarked that consumer attention to an incident or project, or a company’s business model, can concentrate the minds of senior management – and thereby not only raise awareness of human rights but perhaps prompt the company to reorganise its processes and procedures to be able to respond more systematically to the issue. When new issues emerge, they often catch companies by surprise. Such incidents can teach important lessons for the company concerned and other companies in the same sector, as well as civil society, helping all actors to understand how such human rights issues can be addressed in a systematic manner.

Staff need appropriate incentives and disincentives (embedded in a company culture supportive of human rights) to take on difficult discussions with customers.

The Guiding Principles emphasise that a company’s policies and practice need to be internally consistent. Companies participating in the research identified several dilemmas in this area. For example, tensions can arise between sales teams (who want to maintain good relations with customers) and sustainability or compliance teams (who may wish to terminate relations with customers who fail to abide by contractual requirements on ethical, EHS or human rights issues). Human rights are a new issue and may not be seen by all as “hard” enough to terminate relations with customers. One respondent noted the relevance of appropriate incentives and disincentives because, in their absence, “you are asking the sales people to bite the hand that feeds them”. Another reported

the company practice of linking incident reporting to bonuses, e.g. if sales staff observe adverse human rights impacts at a customer site, they are instructed to address the issue and if necessary to stop selling. If they fail to respond, their bonus will be reduced. Another respondent noted that an existing training programme for sales staff on how to deal with integrity issues was being extended to include human rights, but questioned whether relevant staff would feel adequately empowered, supported and incentivised to walk away from business opportunities if a human rights issue comes to their attention.

In addition to incentives, respondents highlighted the importance of a company's culture, noting that as cutting off a customer may "hurt business, it has to be linked to company values or it would never fly".

Regulatory and MSI requirements can be a source of leverage.

Respondents noted that a growing range of regulatory provisions (on export controls, trade rules and environmental regulation) require companies to undertake due diligence or investigation of some kind into customers, with corresponding contractual provisions to address potential liability. Several said that are working to integrate human rights considerations into these systems. As one respondent noted: "we are using hard law examples to signal that soft law issues can become hard law and therefore prevention pays when it comes to customers".

MSI requirements can serve the same purpose by providing a mandatory framework that member companies must apply to their relations with customers. Where the MSI involves both suppliers and customers, such frameworks also create a space within which companies can discuss common conditions of sale with their suppliers and customers. Such initiatives bring together the whole value chain to address issues facing the sector, helping to develop a common approach that can improve company practice across the sector.

The Business Relationship Cycle

Selecting and Starting the Relationship

Setting expectations and communicating them to business partners

Business customers and partners are expressing their expectations on human rights. This can lead to a "battle of standards" that companies are starting to address and avoid.

Consumers as well as business customers are more frequently demanding companies to demonstrate that they have appropriate human rights policies and procedures in place. They noted increasing questions about their human rights approaches when dealing with business customers. This came in the form of general enquiries, requests for specific contractual provisions or requests for compliance with a customer's code of conduct. These demands bring home to managers that they need increasingly to consider human rights as a cost of doing business with their own customers.

Competing policies or codes among business parties to a contract can lead to a “battle of standards” (as to whose code is referred to in contracts) or to a lengthy process to show an equivalence of business codes of conduct. Since most companies prefer to apply their own standards, many regularly benchmark their standards against peers and industry associations to achieve and demonstrate a basic equivalence. One company, for example, does not allow audits by customers, but undertakes to identify gaps and close them, and will discuss the alignment of its own and a customer’s standards.

Consumer expectations on human rights can be a source of leverage that assists companies to raise human rights issues with their business partners.

Consumer interest in human rights issues in product or service value chains, can provide powerful motivation to open a conversation with business partners that use the company’s brand (such as franchisees) about human rights.

Understanding the issues – Assessing human rights impacts in direct customer relationships

“Know Your Customer” processes may address certain human rights issues but do not yet do so systematically.

A range of companies use “Know Your Customer” systems to help them meet regulatory requirements and protect company reputation. To comply with anti-money laundering and corruption laws, for example, companies often need to investigate their customers. Several companies noted that such investigations may include issues relevant to human rights (legal compliance, reputation issues, UN sanctions, criminal or civil litigation, business references, policies and procedures), but human rights are not often considered systematically. Respondents also noted a lack of commercially available information. One company noted that it plans to do a specific gap analysis against the Guiding Principles to ensure that its initial “know your customer” due diligence checklist on customers is up to date.

For companies entering into a large project, knowing the customer and the project is an important part of the company’s assessment of potential reputational risk and is specifically addressed before putting in a bid. Due diligence on customers is often context specific. Companies concerned about dual use of products covered by export controls must take export regulation restrictions on end-users into account. It is important who the customer is: major multinationals with well-developed policies and systems will often receive less scrutiny than small customers whose understanding of company products or services, and capacity to use them appropriately, is unknown. Understanding a customer’s commitment to sustainability may be an important consideration to the seller. Some respondents observed that much depends on the nature of the relationship with a customer: their leverage and ability to impose conditions is less for a one-off sale than for long-term clients.

Businesses that sell directly to consumers can rarely assess individual consumers, because the purchase relationship is not set up for individual interaction. Instead, companies may focus on gaining a more general understanding of their consumers, including their

attitudes to human rights, for the purpose of selling more, and better, products and services. This puts the discussion into the purview of the marketing or product design or product stewardship departments.

Including human rights considerations in standard bidding documents could improve outcomes and level the playing field.

For companies entering into a large project, knowing the customer and the project is an important part of the company's assessment of potential reputational risk and is specifically addressed before putting in a bid. In many cases, bidding documents or purchase agreements are standardised, and allow little scope for adding conditions. This is often true of government contracts (such as public-private partnerships, host government agreements or concession agreements) where they have not begun to reflect their duty to protect in government contracts. Including human rights requirements in large infrastructure contracts would level the playing field for bidders.

Knowing how customers will use products or services is a key challenge.

Customers sometimes misuse a product or service to carry out human rights abuses. Many news stories have examined this issue, notably in the information and communications technology (ICT) and security sectors. In some instances, companies have sold products or services whose misuse was clearly foreseeable (as when a specially designed surveillance software was sold to authoritarian regimes and used to track human rights activists). In others, the end-use was so novel that it could not reasonably have been foreseen. Between the extremes, customer use and misuse take a bewildering variety of forms.

Companies are clearly prohibited from dealing with customers on sanctions lists and export control lists. Beyond this, however, several respondents noted that it was often hard to develop sound human rights due diligence procedures for specific customers. It is particularly difficult, for example, to obtain information on the military and police. One company uses a three-step country-customer-product review against eight prioritised human rights risks.

Companies identified several scenarios that caused particular concern:

- Participating in a large project with little leverage to prevent the products or services that it provides from being misused at a later date.
- A company sells major items of equipment that have a long life span, and has no control over their use after sale (or its exit from the project).
- A company's products are used knowingly and purposefully by a client to do harm.
- Products that resemble a company's own products are knowingly used to do harm.

These are challenging dilemmas for companies that wish to implement the Guiding Principles and assess appropriate responses to their level of involvement in abuses associated with customers' use of their products and services. One respondent noted that it is particularly concerned to understand the circumstances in which, as a consequence of the end-use of its products, it can be said to have enabled human rights

abuses. Companies dealing with products or services that enjoy high brand value and visibility have a particular incentive to ensure that customers use them appropriately. One company does extensive investigations of its customers and imposes detailed requirements on end-use. For another, end-use is a key design consideration: it tries to design its products so that purchasers cannot use them for certain inappropriate or dangerous purposes.

Formalising the Relationship

Company contracts are excluding certain uses of products or services.

Recognising their leverage is often greatest at the beginning of the relationship when deciding whether to do business with a particular customer, participants noted a number of different contractual arrangements aimed at excluding certain uses or users of their products or services that might entail potential adverse human rights impacts:

- Sales agreements prohibit the customer from taking, or providing services for, any actions covered by international sanctions.
- Sales agreements restrict sales to certain types of buyers (such as professional users).
- Contracts reference a list of exclusions, specifying products that are prohibited (that the company will not use or purchase).

Some companies require compliance by customers as a contractual requirement.

In some markets and for some products, sellers are able to set the terms on which customers can use their products. One respondent has standard three-year contracts with customers requiring compliance with their code of conduct that includes a list of relevant human rights conventions. These contractual arrangements are backed up by a system of regular monitoring and management of customers. The contract also includes a 'best endeavours' clause by which customers are expected to apply the respondent's code of conduct to their own customers and significant contractors. In this manner, the respondent significantly extends the potential application of its human rights requirements.

Other models (such as click-through terms of service to which customers must consent when they make an electronic purchase) may contain certain compliance requirements, but provide no opportunity or possibility of being monitored. Several respondents noted that some governments are unwilling to amend standard contracts, or impose conditions on their use of goods and services, despite their duty to protect human rights as set out in Pillar I of the Guiding Principles.

A company may need to take a big picture approach regarding product misuse associated with its name or brands.

Several companies noted that, in certain cases, customer misuse (or longer-term customer use) of a product had a significant impact on human rights, including on the rights to health and to life. Some companies were applying lessons learned and changing their business relationship contracts and conditions to address the human rights risks identified. Other companies were finding they have little leverage and are exploring other ways to influence outcomes. Because companies are often “involved in” the products and services in the meaning of the Guiding Principles, respondents recognised that, to make progress, companies will need to take a big picture approach, involving more players to address customer misuse of a product or service to which the company is directly linked. Different strategies were suggested. Companies might:

- Lobby governments to regulate wider misuse.
- Work with industry associations to address misuse perpetuated or ignored by competitors.
- Work with customers or intermediaries to train end-users on appropriate use of products.
- Work with other players to offer alternative, potentially less dangerous products to certain end-users, like consumers.

Instalment sales contracts and after sales service agreements can provide a measure of leverage over customers’ use of products.

Where customers pay for products in instalments, the company retains some leverage over customer end-use until the last payment is made. Several respondents noted that service or maintenance contracts (for products already delivered) provide similar leverage. If customers are found to be misusing products, some companies have threatened to end further servicing.

Customers may use contracts to shift liability to business partners in a manner inconsistent with the Guiding Principles.

Some respondents noted a concern that standardised sales contracts imposed by customers might shift full responsibility and liability for human rights issues to the seller without a corresponding alignment of costs or other adjustments to risk allocation. They observed that such a practice was out of line with the Guiding Principles as where a direct linkage exists, both parties (to a sales contract) retain a measure of responsibility to prevent and mitigate negative human rights impacts.

Harvard Business Review: 'GE Healthcare in India: An Ultra (Sound) Strategy?'⁹⁶

From the 1970s to the 1990s, Indian doctors used GE's ultrasound technology for a range of diagnostic purposes, including childbirth complications, disease, obstructions, blood flow, heart abnormalities, cancers and, increasingly, emergency diagnostics. The company became aware that the technology was being used to determine the sex of fetuses, and that numerous female fetuses were subsequently being aborted. The case study analysed what GE Healthcare (GEHC) India did to prevent the misuse of its ultrasound machines for prenatal sex determination, which included:

- Increasing the stringency of the sales review process through a combination of training programs, amendments to legal contracts, regular auditing, and rigorous sales screening and tracking.
- Working with Indian government officials to identify proactive ways to educate doctors against misuse, such as with the stickers, labels, PNDT audits and reporting concerns about non-compliance.
- Sharing information with government officials about its internal controls and sales practices that go beyond the current legal requirements and called upon the government to increase enforcement activities and education programs.
- Pushing for industry-wide action.
- Engaging with many of the critical activist group leaders about its efforts to increase safeguards in the sales process to lower the risk of misuse of its ultrasound equipment.
- Running a poster campaign to work creatively on changing attitudes about female feticide and the status of girls and women's rights.
- Designing new CSR programs including social investment in initiatives that promote education and equality among girls in India.

The case study shows both the complexity of customer misuse, how challenging it is for companies to anticipate the full scope of relevant issues in their risk assessments, but also how a company can enhance and apply its leverage through numerous avenues to prevent and mitigate adverse human rights impacts.

96 Jared Harris, Mayank Jain, Jenny Mead, University of Virginia (Oct. 2008). At: <http://hbr.org/product/ge-healthcare-in-india-an-ultra-sound-strategy/an/UV1038-PDF-ENG>; and Business Leaders Initiative on Human Rights (2010), *The Millennium Development Goals and Human Rights: Companies Taking a Rights-Aware Approach to Development*, p. 47.

Managing the Relationship

Risk management approaches can identify which customers require additional attention.

When relationships with the customer are ongoing and longer-term, some respondents adopt tiered risk-management approaches to identify red flags and select high-risk customers for additional investigation and attention. A few respondents noted related multi-step screening processes as a first step to customer use of their products or services. For example, they:

- Screen all customer requests against “usual” requests to identify exceptions that should be flagged for additional investigation.
- Screen customers from high-risk countries more carefully.
- Screen for any breach of sanctions and other potential legal liability issues.

Through applying such series of screens, several companies noted they are able to narrow their focus on customer relationships requiring more serious attention. Some companies add self-declarations to the process to shift the onus back onto customers to state clearly how they will use the company’s products or services.

Ending or Renewing the Relationship

Legacy issues can be a key challenge.

Respondents noted that legacy issues are another key challenge, particularly for a company that sells large pieces of equipment that may outlast its involvement with the customer or its operations. For many participants, “sell and go” is no longer a risk-free option. Several noted that companies need to manage their reputational risk in such cases, and reflect more deeply on their responsibility and liability, because their products and projects can directly and significantly affect a community. Another raised the issue of company responsibility when large equipment or large projects sold later have an adverse impact as a result of the effects of a natural disaster. The assumption that the companies or persons using this equipment will do so responsibly may be changing in light of recent disasters.

One respondent highlighted a dilemma management process to provide more structure to such deliberations. It considers a range of product use issues, from product design considerations, amending due diligence procedures (including human rights due diligence procedures), to contractual requirements, and exit strategies.

Other participants noted that consumers associate sites and products with brand companies long after they exit. This highlights the importance of vetting buyers of assets associated by consumers with the company, even if it remains very difficult to impose post-sale conditions in contracts, or enforce them. Once an asset is sold, a seller would have little leverage to control how the asset is used and whether it continues to be operated to the company's standards.

As noted in Chapter 4 (the Business Relationship Cycle), companies whose projects have a large footprint increasingly consider arrangements for exit, and operations after exit, from the start of operations. Recognising that closure is likely to cause significant decline in both community income and the tax revenue of local government, these arrangements may include establishing sustainable livelihood programmes for the local community that provide for post-closure alternative income generation and sustain the delivery of social services. These programmes can help to ensure that economic, social and cultural rights, in particular, are respected.