BANKS, BUSINESS AND HUMAN RIGHTS

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Global banks and international businesses have now reached a tipping point on environmental, social and human rights issues whereby we can now characterise 21st century international business as being at the dawn of a New Enlightenment based on responsible banking and fiduciary or sustainable capitalism.

THE VANGUARD OF INTERNATIONAL BANKERS AND BUSINESSMEN

To name but a few of the leading bankers and businessmen who are moulding a new world which places the environment, sustainability and respect for human rights at the core of their businesses for good commercial as well as sound ethical reasons: Charles Prince, CEO of Citibank, Martin Hancock COO of Westpac and Chair of the UNEP FI[1],Lord Browne, CEO of BP, Peter Sutherland, Chairman of BP and Goldman Sachs, Henry M Paulson Jr, CEO of Goldman Sachs, Jeff Immelt, Chairman and CEO of General Electric (GE), Sir John Bond and Sir Stephen Green, Chairman and CEO of HSBC respectively have all made important statements to their shareholders on the need for business to embrace sustainability, protect human rights, reduce greenhouse gas emissions, promote new green technologies or to invest funds in a way which considers the relevance and materiality of environmental, social and governance issues in making investment decisions.

Were this mere rhetoric, it would be impressive in its own right. However, those banks and businesses are not paying lip service to the green lobby, international bodies or multistate or state government aspirations for the eradication of global poverty or a better society. Rather, banks and businesses both see the need for change as fundamental to the future prospects and market respect of their businesses and have appointed a cadre of champions to push sustainability through their businesses. Richard Burrett at ABN Amro, Chris Bray at Barclays, Pam Flaherty at Citi, Forster Deibert at West LB and Jon Williams at HSBC, are not only amongst the better known leaders of sustainability in the banking world, but are also as formidable, experienced, and intellectually intimidating an array of financial acumen as you would wish to meet. Each has been given a key role in his or her bank by the Chairman and Chief Executive to make sustainability work within the bank and to ensure in its business practices and decisions that the reputation of the bank is maintained and enhanced.

To illustrate the seriousness with which the leaders of global banks take the concept of sustainable and responsible banking and the uniquely vulnerable position of banks to their clients' activities, it would be possible to cite any number of bank Chairmen, CEOs or Heads of Sustainable Business. Jon Williams, however, expresses their concerns most succinctly when he states that the position of HSBC is that 'no client and no one piece of business is worth risking the reputation of the bank for'. But it is not only HSBC that is setting the highest standards in lending decision-making. Other Equator banks are equally active or are becoming more active in doing so.[2]

On the business side, two leaders, Lord Browne of BP and Jeff Immelt of GE, arguably stand out from the pack. What distinguishes BP and GE from the rest is not only those leaders but the outstanding quality of the people who support them in their commitment to sustainable business. People like Steve Ramsay, Global Head of Environment at GE and Graham Baxter, Vice President Corporate Responsibility at BP, are well known. However, anyone who has worked on the same side or opposite side of these companies will recognise a commitment to the values of the company, a collegiality and depth in quality and expertise which few other teams possess.

BP recently announced that it will make vast investments in alternative energy, and GE's 'ecomagination' has developed further a very strong corporate commitment to improving the environment and developing green technologies. These two global giants are also to be found at the forefront of the development of wind, wave and solar energy technology and are exploring hydrogen energy generation, carbon sequestration and clean coal technology as an increasingly important part of their core businesses.

In addition, the lessons of the BTC pipeline development have been learnt by BP, particularly in respect of human rights protection, whereby BP and Amnesty International have agreed a Memorandum of Understanding in relation to Human Rights. The Memorandum of Understanding attempts to balance those areas of legislative concern which may affect the financial viability of the project over the long run with the need to protect human rights and ensure health and safety as well as non discrimination of those affected by the project. Normally, changes in the law relating to taxes, oil revenues or compulsory acquisition of an energy plant or equipment without full compensation are placed under a moratorium in Host Country Agreements and Inter-Governmental Agreements, which effectively displace for a set period of time the rule of law in order to offer some security to project sponsors. The Memorandum of Understanding, on the other hand, provides that any such suspension of legislative developments will not apply in relation to human rights protection, anti-discrimination or health and safety requirements. It is believed that such factors are not relevant to the financial basis of the project and therefore should not be a matter in respect of which BP should seek exclusion or special protection. Amnesty International are at present trying to negotiate with Chevron a similar Memorandum of Understanding on Human Rights for the Chad-Cameroon pipeline .

The willingness of BP to enter into such agreements with NGOs and its commitment to greater transparency and anti-corruption, as a repeat player in respect of major projects globally, bodes well for BP's future. BP and other oil and gas extractive companies face the challenge of developing projects in environmentally hostile or difficult parts of the developing world. As the world's natural resources are depleted, it will be increasingly important, and banks and civil society will demand, that projects are not only delivered on time and to budget but also with due respect for human rights and the environment. The fact that BP was willing to meet criticism of its enforcement of security measures by organising independent training for security staff on issues of human rights[3] and due process adds to the reasons why BP will be amongst sponsors of choice when it comes to governments and financial institutions selecting which company should be entrusted with major projects.

VOLUNTARISM V REGULATION

There is rather an acrid debate which focuses on whether voluntarism or regulatory initiatives are the best way of achieving desired changes in social behaviour by business. In *A Big Deal?*, for example, the Corporate Responsibility Coalition of the major environmental, human rights and humanitarian NGOs states that 'none of the current array of international CSR initiatives in the finance sector, ranging from the UN Global Compact's Financial Institutions Initiative to the Equator Principles has proved capable of preventing serious problems and abuses they purport to address'. However impressive (and it is argued that they are very impressive) these voluntary initiatives are not a complete substitute for legislative enactments. Rather, they supplement legislation where it is in place and provide a system of norms where such legislation is absent.

There is also a surprising naïvety and trust amongst NGOs about government and laws. It is understandable that liberal economists would wish government and laws to stay right out of the way of business because the market is a more effective allocation mechanism than either but for NGOs to place faith in governments and legislation delivering the goods on the environment or human rights flies in the face of experience and a mountain of jurisprudence and economic texts as to why laws and legal enforcement fail to achieve changes in social and business behaviour.

VOLUNTARY INITIATIVES

These include:

- the 160 financial institutions which are part of the UNEP FI;[4]
- the 2300 business and non-commercial participants in the UN Global Compact;
- the UN Norms on the Responsibilities of Transnational Corporations and other Business Enterprises with regard to Human Rights;[5]
- OECD Guidelines for Multinational Enterprises;[6]
- the 36 major banks and export credit agencies which have adopted the Equator Principles;
- banks and companies such as BP, ABN Amro, Citi, HSBC, JP Morgan, West LB and Goldman Sachs which have come out of the closet and declared themselves for the environment and sustainability;
- GE's 'ecomagination';
- the building of human rights understanding between Amnesty International and BP;
- the companies which have agreed to join the carbon disclosure programme;[7]
- the many FTSE 100 and Fortune 500 pension funds and asset management companies which have incorporated environmental, social and governance ('ESG') issues into their investment mandates and practices. This has been achieved via the Business Leaders Initiative in Human Rights ('BLIHR');
- the Association of British Insurers Disclosure Guidelines on Socially Responsible Investment;
- the Principles of Responsible Investment (to be launched in 2006 by the UNEP FI Asset Management Group).

LEGISLATIVE INITIATIVES

These include:

- some important legislative requirements[8] on pension fund disclosure of how environmental, ethical and social issues are taken into account in investment decision-making in a number of European jurisdictions;
- the French[9] and Australian[10] disclosure requirements regarding social and environmental indicators in Annual Reports and retail investment products;
- Sarbanes-Oxley Act[11] and Securities and Exchange Commission requirements concerning environment impacts and product liability;
- the increasingly important US Accountancy Standards such as FAS 144[12] on the treatment of 'mothballing' sites to avoid environmental clean-up triggers and FIN 47[13] on the quantification of clean up and remediation costs;

As the above lists demonstrate, we now have a powerful and heady mix of voluntary initiatives, professional and sector standards, administrative fiat, legislation, highly effective NGOs who act in unison, greater transparency and faster global communications and an increasingly large number of stakeholders who are prepared to support green agendas by boycotts, demonstrations and withdrawing custom. All of this is propelling business towards a greater respect for sustainability than has been evident hitherto.

STRANGE BEDFELLOWS

Yet there are those for whom acceptance that climate change may be an issue of social concern or that the teachings of Milton Friedman may require re-assessment in the post-Gekko ('greed is good') age represents a betrayal, not a refinement, of capitalist values. If 'the business of business is business' alone in Friedman terms, then there is no place for social investment. In fact, social investment is perceived as the devil's spawn as it diverts the righteous business director from the path of maximising profitability.

Equally, there are those in civil society and the NGO movement on the other side of the political spectrum for whom all these voluntary initiatives amount to mere business hypocrisy or 'greenwash', to use the term favoured by the environmental NGOs. These critics point to free-riding, or inconsistent, Equator Banks which pay lip-service to the Equator Principles and do not practise what they preach. Examples of what are tagged by NGOs as dubious projects include: the Three Gorges Dam, Sakhalin I and II LNG facility, the BTC and Chad-Cameroon pipelines, paper and pulp mills in Fray Bentos, Uruguay, Ecuadorian pipelines, South American gold mines, and Icelandic hydro schemes.

One might add to this Gordon Brown's wanton petulance and imprudence in throwing out years of skilful persuasion of business leaders and no little intellectual effort on Operating and Financial Reporting, complaints about the 'complicity' of business in human rights abuses due to the maintenance of little more than a presence in a country with an uneven or poor human rights record and complaints about a general lack of transparency between the lending institutions and their stakeholders. In this world of ideological purity one step forward is, to borrow from Lenin, truly two steps backwards.

A WAY FORWARD?

Is there a way forward for those who believe that the largely voluntary progress made by international bodies, such as the UN and OECD, and the business community in addressing governance, environmental, ethical, social, and human rights issues should now be accelerated and given a more systematic and legal framework?

The way forward for business, NGOs and civil society is to use what has been achieved so far as a platform to build greater understanding of what each can deliver and what may be sacrificed to enable further progress to be achieved. To test this assertion it is proposed to look at three key issues: the Equator Principles, fiduciary duties of pension fund trustees and complicity by businesses in human rights abuses.

EQUATOR PRINCIPLES

The number of banks which have adopted the Equator Principles (known as Equator Banks) has increased from 10 in June 2003, when the Equator Principles were founded, to almost 40 at the beginning of 2006. The principles have been adopted by financial institutions responsible for over 80 per cent of global project finance but, given the practice of syndication of major project loans, the market penetration of the principles is much deeper. Amongst the leading financial institutions which have adopted them are ABN Amro, Bank of America, Barclays, Citigroup, HSBC, JP Morgan, Mizuho, RBS, West LB and Westpac.

A number of Equator Banks apply the Equator Principles to projects with a capital value of less than US$50m whereas others have extended a form of Equator Principle assessment ('Equator-Lite') to other areas of banking, such as credit finance, or incorporated it into their general sustainable banking programmes.

The Equator Principles require the Equator Banks to categorise projects according to social and environmental impacts, Category A being the most vulnerable and Category C the least vulnerable, and to screen projects according to a number of social and environmental criteria. Where the project is based in middle or low income countries, there is also a requirement to screen in accordance with the IFC Safeguard Policies which are currently undergoing review. Depending on categorisation, there are requirements on borrowers for environmental and social impact assessment, environmental management plans ('EMP') and decommissioning plans, compliance with the EMP and periodic reporting on compliance.

NGOs complain about a lack of transparency and accountability in respect of the application of the Equator Principles and it is clear that there have been some teething troubles and mistakes as the Equator Principles have been bedded into banking practice. However, it is also clear that some of the world's largest financial institutions take this commitment seriously and are devoting resources and manpower to getting it right, and also that export credit agencies ('ECAs') are gaining support from the Equator Banks for their demands of project sponsors to adopt better and more sensitive approaches to social and environmental issues.

It is too early to say if the Equator Principles have been an unqualified success, but they have proved to be a bright shining beacon for responsible banking and have had an influence far outside the relatively narrow world of project finance. Awareness of the need for more rigorous testing of the social and environmental impacts of major projects, including the testing of the Sakhalin II project by EBRD and the ECAs, Memoranda of Understanding on Human Rights (please see above), more appropriate structural and cultural consultation, greater respect for indigenous and vulnerable people, better training on due process and the need to protect human rights from abuse have all been promoted by the Equator Principles.

FIDUCIARY DUTIES AND PENSION FUNDS

Despite the evidence that ESG issues often have a material impact on the financial performance of investments (and, indeed, businesses through their CSR policies often proclaim the importance of these considerations to their own business decision-making), many institutional investors still insist that their legal duties – and, in relation to common law jurisdictions, their fiduciary duties – prevent them from taking such issues into account.

Work done by Freshfields Bruckhaus Deringer, Goldman Sachs and other members of the UNEP FI Asset Management Working Group on the Principles of Responsible Investment points not only to the materiality of such issues in investment decision-making but also to the fact that, where there is a material impact on value, failure to have regard to such considerations may itself be a breach of the fiduciary or other legal duties of pension trustees and managers, managers of trust funds or insurance company investors.

A trustee of a pension fund must be prudent , act for a proper purpose and balance the interests of each class or category of the beneficiaries of the fund. A trustee is not entitled to go on a moral crusade with the funds of the members of the pension fund or to ignore their mandate but the trustee does have broad discretion to diversify according to modern portfolio theory and the courts will not, barring 'crusading'– or fettering discretion by trustees, be willing to second guess business decisions with the aid of 20/20 hindsight.

Given that the worldwide investment industry is worth in excess of US $42trn, provided that the decision remains a financial investment decision, the legal capacity of investors and funds to have regard to ESG considerations can have very important impacts on investment in the 'third world', the development of green technology and industries and decisions as to whether to invest in companies with good or poor ESG track records.

Public sector, listed and private companies, funds and asset managers, such as Groupama, USS, RCM (Allianz Dresner), Hermes, Insight Investment, Mercer, Morley, F&C, Acuity, Calvert, USS, CalPERS, Environmental Agency, the BBC and Post Office pension funds, Citigroup, ABN Amro, BNP Paribas, Nikko, Sanpaulo, Bank of America, Barclays and others are looking at ways of integrating ESG considerations into their investment decision-making.

Institutional investors who hid behind the skirts of fiduciary duties to proclaim the need to maximise profits on each investment can no longer do so on legal grounds and it is doubtful if there is any protection where ESG impacts value on valuation grounds.

The Principles of Responsible Investment will be launched by the UNEP FI Asset Management Working Group in spring 2006. This will be another milestone in the recent trend of the voluntary sector working in partnership with business and developing packages that businesses can then adapt to their practice.

COMPLICITY IN HUMAN RIGHTS ABUSES

The UN Global Compact is a purely voluntary initiative. Principle 1 states that 'businesses should support and respect the protection of internationally proclaimed human rights' and Principle 2 adds to this Principle that businesses should 'make sure that they are not complicit in human rights abuses'.

The key concept in Principle 2 unfortunately is the 'c' word, 'complicity'. The use of this concept of 'complicity' in human rights abuses is unfortunate for a number of reasons, some ethical, and some practical.

First and foremost, complicity will always be linked through Nuremberg and other international criminal trials to war crimes; it is a concept then that comes redolent with very negative values.

Second, it is used very widely to cover direct complicity (active participation), joint venture or indirect complicity (common purpose with human rights violator and providing the means for or knew or should have known of human rights abuse), silent complicity (doing nothing to prevent humans rights abuses) and beneficial complicity (benefiting through human rights abuses by others).

An Office of the High Commissioner for Human Rights briefing paper defines complicity as '*participating in or facilitating* human rights abuses by others … A company is complicit in human rights abuses if it *authorises, tolerates, or knowingly ignores* human rights abuses committed by an entity associated with it, or if the company knowingly provides practical *assistance or encouragement* that has a substantial effect on the perception of human rights abuses'.

This is a conceptual morass which leads to definitional anarchy. It is the approach of Humpty Dumpty who instructed Alice scornfully that when he used a word 'it means just what I choose it to mean – neither more nor less'. By using complicity so widely, its impact and usefulness are undermined. 'Complicity' is an intellectual and jurisprudential quagmire which, like Dartmoor, has sucked many to death by suffocation because of its many dangers. The English Law Commission has abandoned trying to define it twice and other Law Commissions, legal professionals and academics (with the odd exception of bodies such as the RAND Institute for Civil Justice and Amnesty International (who should really know better)) have long since abandoned as futile any attempt to make sense of the concept.

Third, on a practical level, if a business is to be held to be 'complicit' when it does not actively or indirectly participate in human rights abuses, it is arguable that there is little or insufficient incentive for business to change its practices. Banks and businesses accept that they should be held responsible and accountable for their actions where they can be shown to have participated or given implicit consent for environmental, human rights or other abuses. This is clear, for example, if we look at the fact that businesses, such as Nike and the oil and gas, extractive and energy industries, are using consultants such as Achilles to clean and green their supply chains and whatever lies within their immediate sphere of influence.

Stuffing and mounting a CEO or Chairman of a multinational business or global bank, may, on occasion, be appealing to the odd NGO but is not generally acceptable. What civil society and NGOs must consider is what they want: real changes in business practices or show trials with the occasional director of a company spending time in an open prison. If it is the former, standards can be hedged with 'best practice', 'due diligence' and 'state of the art' defences or mitigating factors which would reward the good companies and business directors and penalise the bad. Thus BP's decision to obtain professional experts to train the security staff protecting pipelines in due process and respect for human rights might be weighed in the balance against any human rights abuse by security staff, whereas companies that have not trained their security staff in due process and respect for human rights would not be allowed to avail themselves of this defence or plea in mitigation.

Failure to give banks and their customers the ability to buy into human rights in a way which they understand and can respond to – by creating processes, practices and procedures, toolboxes and training, by monitoring and improving performance – all things that business can do and do well – will be a missed opportunity not only for business, civil society and NGOs but also for the vulnerable communities for which protection against human rights abuses is needed. Sometimes a tick in a box is more valuable than scalping a CEO or COO but it is difficult sometimes to appreciate that form can be more important than ideological purity.

CONCLUSIONS

Business is at the foothills of the 21st century but, to borrow from Sir John Bond of HSBC, is looking up at the mountains. Like the Tory leadership, business is casting off the legacy of Thatcher and Friedman, not on purely ideological grounds but because business is looking to providing sustainable profits for this and the next generation.

It is amazing how far business has come so quickly. It is a little less than 10 years ago that Lord Browne of BP made his first public speech on climate change and global warming and it is only five years since Tony Blair bemoaned the lack of interest shown by the FTSE 100 companies on Corporate and Social Responsibility. Not all businesses, it should be said, agree with the approach taken by companies like BP, GE and Goldman Sachs. Indeed, the directors of Goldman Sachs, in adopting an environmental policy to apply to its business decisions, have been threatened with legal action by a leading US fund for failing to discharge their fiduciary duties to their shareholders.

Civil society should think back to the film *Wall Street*, in which Gordon Gekko proclaims that 'lunch is for wimps' – a strange echo of Friedman's observation that 'there is no such thing as a free lunch' – and support the efforts of BP, HSBC, Citigroup, Goldman Sachs, ABN Amro and GE in attempting to develop a new business world. This is not an exclusively green world but one where sustainability of the environment, society and profits is paramount. Businesses are not charities or Victorian philanthropists. They are in competition with each other for scarce resources and profits. The trick is to make them understand the parable of the rich man.

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1 United Nations Environment Programme Finance Initiative.

2 The Equator Principles are a set of voluntary guidelines that were originally adopted in June 2003 by 10 banks and which, by the beginning of January 2006, had been adopted by 36 financial institutions (34 banks, one export credit agency (ECA) and one development finance institution). The Equator Principles apply to all industry sectors and to project finance loans with a total capital cost of over $US50m. They provide a framework, based on the World Bank and International Finance Corporation (IFC) Safeguard Policies, which commits each of the Equator Banks to develop its individual policies, practices and procedures to ensure that projects are assessed according to specific social and environmental considerations and are carried out in a socially and environmentally responsible manner.

3 In February 2004, the Baku-Tbilisi-Ceyhan (BTC) and South Caucasus Pipeline (SCP) projects operated by BP entered into a partnership with Equity International (EI) to support the delivery of training about human rights to state security organisations which are responsible for pipeline security. The training programme has since been launched in Azerbaijan and Georgia.

4 UNEP FI is a global partnership between UNEP and the financial sector. The institutions involved in UNEP FI's work (including banks, insurers and fund managers), work with UNEP to assess and comprehend the impacts of environmental and social considerations on financial performance.

5 Written in consultation with unions, business and NGOs, the UN Norms on the Responsibilities of Transnational Corporations and Other Business Enterprises with Regard to Human Rights, were adopted by the UN Human Rights Commission in August 2003. The norms can be used by human rights advocates, companies and governments and referred to by national and international tribunals. The norms are not an international treaty, and therefore do not require ratification and are not legally binding on states or corporations. But for the most part, they draw on existing human rights law and principles.

6 The OECD Guidelines are recommendations for multinational enterprises operating in or from adhering countries. They provide voluntary principles and standards for responsible business conduct in a number of areas such as employment, human rights, environment, disclosure, combating bribery etc).

7 Please note that in the third cycle of the carbon disclosure project, the information request was signed by 155 institutional investors. Further information is available on http: //www.cdproject.net

8 For example, the obligation imposed on pensions funds in the UK by the Occupational Pension Schemes (Investment) Regulations 2005 SI 3378, 2005 to provide a Statement of Investment Principles (stating whether, and to what extent, ESG issues were taken into consideration when making investment decisions); or the draft Law no.243 of 23 August 2004 which is currently being debated in the Italian parliament and which will require pension trustees to indicate in their annual accounts and reports if, and to what extent, priority has been given to social, ethical and/or environmental considerations.

9 Mutual funds in France, for example, are required to report in their rules and prospectus, the precise criteria used to analyse ESG considerations; whether their management company consults external specialised valuation agencies, and describe the implementation of the ESG considerations in their annual reports.

10 The Australian Financial Services Reform Act 2001 (Cth) introduced a new part 7 into the Corporations Act. The reforms require (among other things) issuers of financial products to give retail clients a Product Disclosure Statement (PDS) containing specified information on the service or product supplied. The PDS must disclose, inter alia, 'the extent to which labour standards or environmental, social or ethical considerations are taken into account in the selection, retention or realisation of the investment'.

11 The Sarbanes-Oxley Act and related Regulations require a public company to disclose (and company officers to certify the accuracy of such disclosure) 'material' costs and liabilities associated with the following environmental provisions: costs of compliance with all enacted or adopted environmental regulations; costs associated with legal proceedings of enforcement actions or 'superfund liability'; and costs associated with 'any known trends, demands, commitments, events or uncertainties' (which almost certainly includes climate change).

12 Financial Accounting Standard (FAS) 144 covers Accounting for the Impairment or Disposal of Long-Lived Assets.

13 The Financial Accounting Standards Board (FASB) Interpretation No. 47, *Accounting for Conditional Asset Retirement Obligations* (FIN 47).

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