

# Corporate duty to respect



## The relevance of private finance

A BankTrack discussion paper

*BankTrack, a network of 27 civil society organisations tracking private finance, submits this discussion note to the Special Representative of the Secretary-General on human rights and business (SRSG), professor John Ruggie, to explore issues relative to commercial finance and the "corporate duty to respect". It represents a non-exhaustive discussion on expectations placed upon private financial actors and practical implications of a duty to respect. We hope this will be informative and assist Professor Ruggie in determining his views and recommendations his mandate.*

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### **Private finance: a duty to respect**

This paper will concentrate on what the duty to respect means in practice, and how it might be operationalized in a manner meaningful to business. According to obligations under national law derived from state commitments under international statutes, corporations have varying degrees of a duty to respect. Many of these were recognised in the SRSG's interim report mapping human rights obligations.<sup>i</sup> BankTrack has briefly dealt with the state duty to protect relative to private finance in a previous discussion note so this paper will concentrate on the enforcement of human rights on with respect to action at the corporate level and at the international level.<sup>ii</sup>

### **Origins of a duty to respect**

Ignoring for a moment the legal context, victims of human rights abuses and society at large tend to focus on private financial institutions duty to respect following (1) an expectation on financial institutions to do no harm, especially when utilising other people's money and (2) that victims be granted access to justice for financial institutions in light benefits accrued to banks.<sup>iii</sup>

Both robust social expectations and responsibility to do no harm are recognised by banks. By establishing their own human rights protocols and guidelines, which in many cases conform with existing international standards such as the *Universal Declaration of Human Rights* and a range of other conventions incorporating human rights obligations. Due to consumer expectations, unfortunately corporate responsibility and public relations have historically been difficult to separate, with many corporate responsibility departments exhibiting closer links with public relations rather than internal governance. It follows that for institutions attempting to address the issue of a duty to respect, what attracts most criticism is cases where human rights considerations are clearly not operationalised into business practice.

Leverage inherent in private financial actors manifests itself in networks such as BankTrack. BankTrack member groups recognise the value in altering financial institution behaviour. Start up capital for projects, advisory services (for operators and investors) are vital requirements for functioning services. With influence over private finance you have supply chain leverage over perpetrators of human rights abuses. The essential role played by private financiers has created legal and expectational responsibilities to the extent that individual banks are creating their own human rights policies and international bodies such as United Nations Environment Program Financial Initiative (UNEPFI) and Global Compact have created guidance tools for private banks.<sup>iv</sup> Unofficially, when financial institutions are approached by concerned members of society, they are typically open to discuss or at minimum listen to victims and their representatives.<sup>v</sup>

Released in December 2007, BankTrack's *Mind the Gap* report rates the publicly available policies of 45 banks against what is considered best practice for financial institutions regarding current tools and international standards.<sup>vi</sup> It was found that 12 of these institutions have developed specific human rights policies. Of the 14 sectors and issues addressed by *Mind the Gap*, many relate to the broad spectrum of human rights. Of note are Labour, which four banks had developed specific policies, Indigenous, five banks exhibiting policies and arms and military industry and arms trade, of which 12 banks had policies. Mind the Gap also recognises that mining, logging, oil and gas as high risk sectors for which banks must incorporate human rights considerations into policy.

On human rights policies, one bank scored 3 out of a possible 4 which indicates the bank's policy defines a clear bottom-line on human rights-related activities and practices which will not be financed AND requires a meaningful Human Rights Impact Assessment for relevant transactions, sectors and countries. Thirty banks scored 1 out of a possible 4, meaning their policy is vaguely worded or aspirational, for instance by endorsing the *Global Compact* or the *Universal Declaration of Human Rights*, with no clear commitments. The remaining 15 banks received a 0 meaning that no human rights policy was in existence.<sup>vii</sup>

Sophisticated screening, exclusion and engagement practices are continually being developed in financial institutions who understand that the duty to respect is an essential part of business practice, and that financial institutions can secure profits and performance by rigorously applying human rights responsibilities to a range of financial services and products. Netwerk Vlaanderen in conjunction with BankTrack is collating instances of best practices which will feature in a report released in the first half of 2008. We invite you to peruse this for background on what the corporate duty to respect means in practice for private financial institutions actively engaging themselves on this issue.<sup>viii</sup> A range of ways banks can influence clients are explored in *Human Rights, Banking Risks*. The methods include exclusion, due diligence, human rights impact assessment, standards (policies), financial covenants, monitoring and corrective actions.<sup>ix</sup>

### **Sphere of influence**

Introduced by the Global Compact, the concept of sphere of influence relates specifically to the ability of a financial institution to have a positive impact on clients or its supply chain. The Office of the High Commissioner on Human rights considers a range of factors effect the sphere of influence. They include as political, contractual, economic and geographical proximity, as well as the size and strategic significance of the company.<sup>x</sup> Other commentators note that the nature of the company's operations, the industry or industries it engages in, as well as its corporate structure is relevant.<sup>xi</sup>

However, what we have noted in practice, is what should be positive enabling factors to influence, are often cited by financial institutions as reasons to continue with a certain relationship in the *status quo*, disregarding human rights considerations. There are many instances where long business relationships are put forth by financial institutions informally to the BankTrack network as the reason why no positive influence could be exerted by them on their clients.

Similarly, the size of a financial institutions is expected to increase the ability to influence a client or business partner, Smaller financial institutions have an easier

time tracking assets and incorporating screening and engagement criteria to increase their sphere of influence. Increasingly we see that the decentralised decision making procedure and lack of inter-departmental transparency decrease a financial institution's ability to positively influence its clients. Above all, it is a willingness to implement human rights criteria at board level and middle management that is the key to expanding sphere of influence. An awareness of issues, risk sectors, risk countries and integrated procedure and a desire to promote the corporate duty to respect internally we note is the most effective way for financial institutions themselves to do this.

### **Existing initiatives**

It is clear that existing initiatives do not sufficiently address human rights considerations for financial institutions. The Equator Principles have limited scope of human rights and application is restricted to project financing. They are not considered to be an adequate substitute to address the duty to respect. It is exactly this reason why financial institutions themselves are developing human rights policies. We agree with the SRSG's comments that the current voluntary framework contains inherent weaknesses and limitations.<sup>xii</sup> Victims have ad-hoc access to financial institutions regarding any manner of human rights affectations, and no official mechanism exists to enforce these rights, and despite granting victims or their representatives and audience, bank responses to implement duties are inadequate in the eyes of the victims.

Investments by 121 transnational financial groups in operations that have seriously impacted human rights have been detailed in a report by BankTrack members Network Vlaanderen. This dossier provides ample evidence of how financial institutions are not complying with the corporate duty to respect.<sup>xiii</sup> It illustrates numerous ways, including but not limited to revolving credit facilities, short term loans, bridge loans, initial public offerings, underwriting, shareholdings and share offerings whereby companies are provided with direct means to raise capital to finance and develop projects with significant human rights impacts. Many of these banks have human rights policies, and you can see how aspirational policies stack up in terms of real life investments in eight bank profiles accompanying the report.<sup>xiv</sup>

Expectations have evolved to the point that where a financial institution is assisting capitalization of a company, and that company is involved in human rights abuses, then the bank must address it. Whereas many banks may only wish to track investment risks to specific projects in the case of project finance lending, there is a clear move to apply human rights criteria to all sorts of financing. The reasoning behind this is varied. Some investors like the Norwegian Government Pension Fund choose to implement an exclusion policy to avoid the risk of complicity in human rights violations.<sup>xv</sup>

BankTrack encourages banks to develop their own human rights policies with the view that rigorous internal implementation of policies which reflect existing international human rights standards can play a positive role to advance the corporate duty to respect.<sup>xvi</sup> Evidently, the desire for business to protect themselves from criticism and legal ramifications inspires the organic construction of industry standards and a level playing field. This is evident through the creation of individual policies as well international initiatives such as the Global Compact. However, business cannot go it alone, and for a true level playing field, global standards on

accountability and responsibility with an independent assessment or enforcement mechanism is the logical way forward.

Given the discussion above, we provide the following suggestions which we hope will be useful for your views and recommendations:

- (1) Universal standards reflecting existing international human rights norms, and enforceable by an independent mechanism is in our view the most effective and desirable means of ensuring the corporate duty to respect is fulfilled. Independent oversight and accountability is crucial to provide incentive for compliance and accessibility for victims, providing a level playing field with uniform international standards already reflected in international instruments representing the normative benchmark.
- (2) Governing actions of financiers through internal policies and procedures is a starting point for the duty to respect, but enabling access to justice for victims may be considered the true litmus test. For many western financial institutions there is an informal willingness to meet with victims affected and non-government organisations. These meetings are often lauded in annual reports as an indication of respecting human rights. In some cases these interest groups are carefully selected by financial institutions posing a danger of co-opting engagement space of affected communities. Providing access to justice for victims to the financiers is a laudable step and should be recommended to financial institutions.
- (3) Practically speaking, many tools are available for financial institutions to facilitate efforts in fulfilling the duty to respect. Workable steps outlining the implementation of Human Rights considerations into bank policy and practice are provided in the publication *Human Rights, Banking Risks*. A range of Human Rights Impact Assessment tools are available for these institutions, and working governance models are exhibited by various financial institutions.<sup>xvii</sup> Encouraging greater use of these tools across a broad range of financial transactions is welcome.
- (4) For financial institutions the duty to respect should apply to all forms of financing, thus extending beyond project finance. Many institutions are addressing the duty to respect with sophisticated human rights policies and broad implementation. It is erroneous that human rights for financial institutions be viewed through the prism of current voluntary initiatives. The failure of the Equator Principles to apply to all methods of financing and cover a range of human rights precludes this from happening. Equally, implementation of the Global Compact commitments into management procedures, despite the available briefing papers, remains altogether too vague and unworkable as a guide for financial institutions to implement. For this reason, universal and independently enforceable standards are welcomed.
- (5) We welcome guidance on grievance mechanism for project proponents. The responsibility on the corporation to implement such a mechanism is fraught with possibilities of misuse. Independence is a key requirement to oversee the operation of a grievance mechanism for community issues. Similarly, a second tier oversight mechanism to enforce the requirements of the grievance

mechanism, such as one that would apply to financiers who oblige their clients to implement such procedures, is essential for responsibility and accountability.

We hope that information and suggestions included in this paper will contribute to the discourse on state duty to protect and the SRSG's views and recommendations.

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# References



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- <sup>ii</sup> *State duty to protect: a BankTrack discussion paper*, November 2007. Available at <http://www.business-humanrights.org/Documents/Submissions-to-John-Ruggie>
- <sup>iii</sup> For more information see *Human Rights, Banking Risks: Incorporating human rights obligations in bank policy*, BankTrack February 2007. [http://www.banktrack.org/doc/File/banks%20and%20human%20rights/banktrack%20on%20human%20rights/0\\_0\\_070213%20human%20rights%20Banking%20risks.pdf](http://www.banktrack.org/doc/File/banks%20and%20human%20rights/banktrack%20on%20human%20rights/0_0_070213%20human%20rights%20Banking%20risks.pdf)
- <sup>iv</sup> United Nations Environment Program Finance Initiative, Human Rights workstream [http://www.unepfi.org/work\\_streams/human\\_rights/index.html](http://www.unepfi.org/work_streams/human_rights/index.html)  
*A guide for integrating human rights into business management*, Business Leaders Initiative on Human Rights / Global Compact  
[http://www.unglobalcompact.org/docs/issues\\_doc/human\\_rights/guide\\_hr.pdf](http://www.unglobalcompact.org/docs/issues_doc/human_rights/guide_hr.pdf)
- <sup>v</sup> Evidence of accountability processes within financial institutions can be found in *Mind the Gap*, p101 to 103. Four out of 45 banks reviewed had established a third-party grievance mechanism.
- <sup>vi</sup> *Mind the Gap*, BankTrack, December 2007
- <sup>vii</sup> *Mind the Gap*, pp72- 77
- <sup>viii</sup> For more information, contact Luc Weyn of Netwerk Vlaanderen at [luc@netwerk-vlaanderen.be](mailto:luc@netwerk-vlaanderen.be)
- <sup>ix</sup> *Human Rights, Banking Risks: Incorporating human rights obligations in bank policy*, BankTrack February 2007, pp16-20 [http://www.banktrack.org/doc/File/banks%20and%20human%20rights/banktrack%20on%20human%20rights/0\\_0\\_070213%20human%20rights%20Banking%20risks.pdf](http://www.banktrack.org/doc/File/banks%20and%20human%20rights/banktrack%20on%20human%20rights/0_0_070213%20human%20rights%20Banking%20risks.pdf)
- <sup>x</sup> *The Global Compact and Human Rights: Understanding Sphere of Influence and Complicity - an OHCHR Briefing Paper*, December 2004 [http://www.unglobalcompact.org/Issues/human\\_rights/gc\\_and\\_human\\_rights.pdf](http://www.unglobalcompact.org/Issues/human_rights/gc_and_human_rights.pdf)
- <sup>xi</sup> <http://blogs.law.harvard.edu/ugasser/category/sphere-of-influence/>
- <sup>xii</sup> *Business and Human Rights: Mapping International Standards of Responsibility and Accountability for Corporate Acts*, Report of the Special Representative of the Secretary-General (SRSG) on the issue of human rights and transnational corporation and other business enterprises, February 2007, paragraph 74
- <sup>xiii</sup> *Bank Secrets: banks and their alarming investment practices*, Netwerk Vlaanderen in association with BankTrack, December 2007. [http://www.netwerkvlaanderen.be/en/files/documenten/publications/reports/bank\\_secrets\\_11\\_12\\_07.pdf](http://www.netwerkvlaanderen.be/en/files/documenten/publications/reports/bank_secrets_11_12_07.pdf)
- <sup>xiv</sup> [http://www.netwerkvlaanderen.be/en/index.php?option=com\\_content&task=view&id=320&Itemid=243](http://www.netwerkvlaanderen.be/en/index.php?option=com_content&task=view&id=320&Itemid=243)
- <sup>xv</sup> *Ethical Guidelines for the Norwegian Government Pension Fund*, available at <http://www.regjeringen.no/en/dep/fin/Selected-topics/andre/Ethical-Guidelines-for-the-Government-Pension-Fund---Global-/The-Ethical-Guidelines.html?id=434894>
- <sup>xvi</sup> BankTrack is currently mapping innovative human rights policies and will release a report in the first half of 2008 For more information contact Luc Weyn, Netwerk Vlaanderen. [luc@netwerk-vlaanderen.be](mailto:luc@netwerk-vlaanderen.be)
- <sup>xvii</sup> HRIA tools and guidance are available from the Danish Institute for Human Rights, Business Leaders Initiative on Human Rights, International Alert, Rights and Democracy. Source: *Guide to Human Rights Impact Assessment and Management: road testing guide*, International Finance Corporation, p6 available at [http://www.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/p\\_SocialResponsibility\\_HRIARoadTesting/SFILE/Final+HRIA+road-testing+draft.pdf](http://www.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/p_SocialResponsibility_HRIARoadTesting/SFILE/Final+HRIA+road-testing+draft.pdf)