

# GLOBAL BANK REVIEW: HUMAN RIGHTS DUE DILIGENCE AND BANKING - A PRACTICAL INTRODUCTION

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Scrutinising human rights records is moving into the mainstream of deal-making. That will include lenders.

This article is part of our [2021 Global Bank Review - ESG: Creating a purposeful future](#), an annual publication by our Global Banks Sector Group which brings together our people who live and breathe banks.

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When human rights become a core business consideration – as they unquestionably have over the last decade – the lending community cannot long avoid engaging. After all, banks can have huge influence in corporate practice through lending decisions and the conditions upon which lenders make finance available, helping to move such matters from tick-box compliance to mainstream funding strategy.

In response, an increasing number of banks are making human rights due diligence part of their business. It can also be a key tool to understand and manage lenders' ESG risks and incentivise better standards throughout the business community.

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## THE ROAD TO HUMAN RIGHTS DUE DILIGENCE

Human rights due diligence (HRDD) is a fundamental aspect of a company's responsibility to respect human rights. In 2011, the UN Human Rights Council unanimously endorsed the United Nations Guiding Principles on Business and Human Rights (the UNGPs), reflecting global consensus that all businesses should respect human rights. Alongside creating and implementing a policy commitment to respect human rights and an effective remediation process, HRDD is one of the core steps a company should take to act consistently with the UNGPs.

While the UNGPs themselves are seen as international 'soft law' – and not directly binding on companies – they have in recent years precipitated a number of mandatory domestic laws on human rights issues. Examples include the UK and Australian Modern Slavery Acts, the French law on the corporate duty of vigilance, the German supply chain law and a corporate human rights law in Switzerland. There have also been moves towards the introduction of legislation seeking to ban the import of goods produced using forced labour.

Most significantly, the EU is currently considering the introduction of a new regime for companies to undertake mandatory human rights and environmental due diligence. The text of a draft EU directive approved by the European Parliament draws heavily from and is closely aligned to the UNGPs. If a law comes into force in those terms, soft law standards on HRDD may quickly solidify into prescriptive legislation.

The UNGPs, including the concept of human rights due diligence, are also embedded in other international standards, such as the OECD Guidelines for Multinational Enterprises, OECD guidance on Due Diligence for Responsible Corporate Lending and Securities Underwriting, the IFC Performance Standards and the Equator Principles. An increasing number of banks have publicly committed to implement these standards in their operations.

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## **WHY IS IT IMPORTANT?**



**“An increasing number of banks are making human rights due diligence part of their business.”**

Access to finance has the potential to assist in fulfilling a wide range of fundamental human rights. Likewise, the activities of a bank and its value chain can significantly impact a broad range of human rights. Apart from the general importance of respecting human rights, a bank may need to undertake HRDD to ensure alignment with any policies and/or public commitments it has made. Robust HRDD will also help a bank identify, understand and manage the legal and reputational risks that its business (including lending) has caused or contributed to adverse human rights impacts. HRDD, moreover, supports compliance with the increasing reporting obligations banks are facing and can be a part of an effective sanctions compliance regime.

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## WHAT DOES HRDD INVOLVE?

According to the UNGPs, HRDD should be ongoing and should involve a company:

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- identifying and assessing its potential adverse human rights impacts;
- integrating and acting upon the findings;
- tracking responses; and
- communicating human rights performance externally.

A key aspect of HRDD is disclosure. Most domestic regulation in the area of business and human rights has so far focused on reporting and transparency, without necessarily mandating due diligence. However, substantive reporting to a sophisticated audience is extremely difficult without first carrying out HRDD. As a result, there has been a trend in recent years towards increased transparency. The idea behind this approach is to provide a measure of transparency and accountability to individuals or groups whose rights may be impacted and to other relevant stakeholders, including investors.

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## **THE IMPORTANCE OF A CROSS-FUNCTIONAL APPROACH**

Human rights considerations also impact and interact with other issues. For example, while the objective of a sustainable loan may be linked to an emissions reduction, it is important that human rights are also respected in this context. This will be even more important if the EU goes ahead with proposals to expand the Taxonomy Regulation – an ambitious attempt to classify which economic activities qualify as sustainable – to include social objectives such as human rights.

The increasing global focus on climate change is also relevant; human rights arguments are being increasingly deployed in climate change litigation as climate change has been recognised as impacting on a wide range of human rights.

In summary, a bank's approach to human rights and HRDD should not be tackled in isolation. Instead, institutions should ensure such issues enter the mainstream of their decision-making and that human rights factors are fully integrated with broader assessments of ESG issues. Whether convert or sceptic, all lenders will soon need a coherent human rights approach.

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