

NEXT DECADE | 10+



UNITED NATIONS  
**HUMAN RIGHTS**  
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# Taking stock of investor implementation of the UN Guiding Principles on Business and Human Rights

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Adendum report of the Working Group on the issue of human rights and  
transnational corporations and other business enterprises

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# Executive summary

In the run-up to the 10th anniversary of the UN Guiding Principles on Business and Human Rights (Guiding Principles), the UN Working Group on transnational corporations and other business enterprises (Working Group) launched the “Guiding Principles 10+ / Next Decade BHR Project.” The Project assesses the first decade of implementation of the Guiding Principles by States and business enterprises and aims to develop a roadmap for meaningful action in the decade ahead.

In recognition of the need to promote the investor responsibility to respect human rights, including as a key means to speed and scale up business respect for human rights, the Guiding Principles 10+ project shines a brighter light on the role of institutional investors – asset owners and managers – in *Taking stock of investor implementation of the UN Guiding Principles on Business and Human Rights*.

This report provides a summary of what rights-respecting investment entails, based on the expectations of the Guiding Principles, the authoritative global framework for the respective duties and responsibilities of governments and business enterprises to prevent and address business-related human rights impact. It outlines how enabling environments have fostered greater investor respect for human rights over the past decade and summarises signs of progress as well as major gaps and barriers to future progress. It wraps up by providing a set of recommendations for increasing investor action over the course of the next ten years and beyond, concluding that a widespread and serious embrace of long-term thinking and decision-making within investment institutions and the full spectrum of actors they work with is an essential and core component of upholding the dignity and wellbeing of individuals and communities.

## ***Enabling environments for rights-respecting investment are emerging***

The report highlights that progress in investor uptake of the Guiding Principles over the past decade has been bolstered by increased efforts from certain standard-setting bodies seeking to create an enabling environment for rights-respecting investment. These actors – including governments, multilateral organisations, reporting frameworks, industry associations, multi-stakeholder platforms, and stock exchanges – play a critical role in driving Guiding Principles implementation at scale and facilitating a level-playing field for investors. The European Union (EU), in particular, has taken on a leadership role in redefining the responsibilities of institutional investors by ensuring that environmental, social and governance (ESG) considerations, including human rights, are at the heart of the region’s financial system. A wide range of research over the past decade has also documented the correlation between human rights risks, corporate financial performance and risks to investment and helped bolster investor engagement on human rights, while industry initiatives have started providing much needed collective action platforms to activate investor action to promote the uptake of the Guiding Principles.

Despite this progress, uptake of the Guiding Principles among governments and standard-setting bodies has at the same time been inconsistent and insufficient. There is widespread misalignment between legal frameworks for investment decision-making and the Guiding Principles, as well as weak enforcement of existing environmental and social requirements where these exist. There remains a capacity gap across State institutions and within multilateral entities, including the United Nations, when it comes to speaking out about investor responsibility and accountability in relation to human rights.

## ***Progress and gaps of investor uptake***

While engagement with human rights issues among socially responsible investors has a longstanding history, the shift in approach to aligning investment practices with international standards such as the Guiding Principles has only recently begun. Human rights policy commitments are growing in number among investors and human rights reporting frameworks and benchmarks are supporting their efforts to assess and engage companies on human rights. Investors are also activating their leverage to engage companies

on the uptake of the Guiding Principles among portfolio companies. For example, investors representing \$5.8 trillion in assets have called on companies to improve their rankings on the Corporate Human Rights Benchmark. Shareholder resolutions increasingly call on companies to implement the Guiding Principles, and some of the world's largest asset managers have cast votes in favour of human rights due diligence in the past two years. While still exceedingly rare, some investors are making increased efforts to enable access to effective remedy for victims of business-related human rights abuse.

Despite progress, human rights are still rarely addressed in a systematic or principled way among the institutional investor community. The vast majority of investors have yet to meaningfully engage with their human rights responsibilities. Most investors have significant capacity challenges with regard to business and human rights. As a result, knowledge of human rights, including how human rights are defined, how they are relevant across ESG factors, and what meaningful human rights due diligence looks like, remains limited throughout the institutional investor community. Even areas of investor activity where consideration of social impacts are seemingly embedded have been largely detached from efforts to align investment activities with the expectations laid out by the Guiding Principles. This includes in the context of impact investing, which seeks to generate positive social and environmental impacts alongside financial returns and investing toward achievement of the Sustainable Development Goals (SDGs). The ability of investors to meaningfully assess and prioritise human rights risks connected with their investment activities has also been challenged by the fact that meaningful corporate human rights disclosure has been the exception, not the norm, over the past decade. A root cause of this has been the inconsistent integration of the Guiding Principles across the myriad reporting frameworks, benchmarks and other data and research products used by investors to assess companies.

A culture of corporate short-termism, therefore, still prevails in financial markets with devastating impacts on human rights and the environment. Increased shareholder pay-outs and compensation for executives and directors tied to short-term financial performance has been coupled with cost-cutting and wage stagnation for workers. Investor pressure, especially from hedge funds and private equity firms underlies this trend, though pension funds, sovereign wealth funds, and even union funds are participating in riskier forms of investment in order to meet their commitments to beneficiaries.<sup>1</sup>

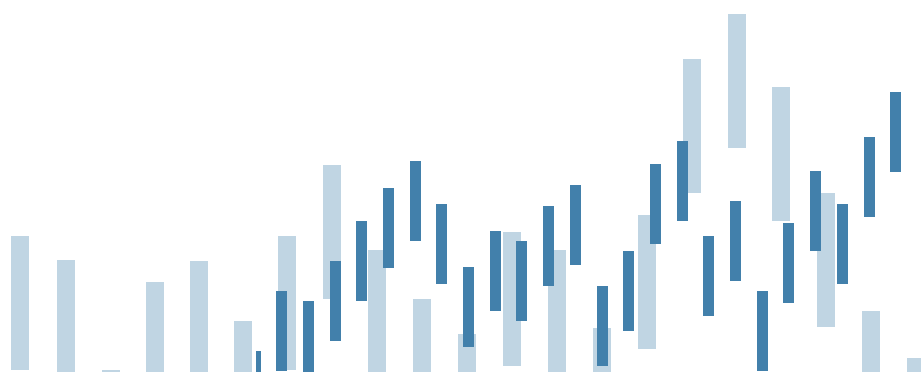
The report concludes that efforts to achieve the widespread implementation of the Guiding Principles throughout the economy will continue to be stymied unless investor respect for human rights is sped and scaled up. The following list is an excerpt of recommendations for (1) States, (2) institutional investors and (3) other actors in the investment ecosystem to advance the investor responsibility to respect human rights over the course of the next decade, and beyond.

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<sup>1</sup> Source: <https://www.hks.harvard.edu/sites/default/files/centers/mrcbg/files/EU%20HRDD.pdf>

## Recommendations for States

- Ensure that State institutions dealing with institutional investment have the mandate, skills and resources to promote investor respect for human rights.
- Support the creation of guidance for institutional investors, including public pension funds, sovereign wealth funds, development finance institutions, as well as small and medium-sized investment firms, on respecting human rights throughout their investment activities, including on how this relates to fiduciary duties and to broader sustainability and ESG investing.
- Support, facilitate and participate in multi-stakeholder platforms to promote dialogue on institutional investment and human rights, analyse ways to address human rights risks in investment activities and strengthen monitoring and accountability.
- Develop and implement policies for cross-government alignment of UNGPs implementation activities with legislative, regulatory, policy and adjudicative efforts related to institutional investment.
- Commit to specific, future-oriented actions to promote respect for human rights among institutional investors and their ecosystem, for example, in national action plans on business and human rights.
- Promote policy coherence regarding the human rights responsibilities of investors in the context of State institutions tasked with promoting sustainable economic development. Particular attention should be placed on the role of investors in encouraging companies to carry out human rights due diligence as the first step towards the realisation of the SDGs.
- Integrate respect for human rights into the mandate, operations and investment activities of institutions involved in the issuance and management of State pension funds, sovereign wealth funds and development finance.
- Strengthen implementation of relevant legislation and codes, including ESG requirements for asset owners and asset managers, and clarify how these relate to human rights.
- Mandate corporate (investee) human rights due diligence in line with the UNGPs to support investors' efforts to assess and address human rights risks in investment portfolios. To the extent that the State requires companies to exercise human rights due diligence, these requirements are inclusive of institutional investors and financial institutions in general.
- Address investor short-termism and encourage longer-term investments, for example, by imposing greater taxes on short-term capital gains relative to long-term capital gains, reforming disclosure requirements to align with longer periods of time and placing greater scrutiny on derivative trading or other practices/products that contribute to short-termism.



## Recommendations for institutional investors

- Articulate a commitment to respecting human rights and embed this commitment in corporate governance and across all investment activities. Embed the commitments throughout the investment firm, for example, by hiring in-house human rights expertise, training staff tasked with investment decision-making and stewardship on human rights, ensuring performance targets do not hinder human rights due diligence and integrating the human rights commitments into other investment policies, codes of conduct and limited partnership agreements.
- Assess the actual and potential human rights impacts of investees prior to investing and on an ongoing basis once invested. This involves assessing the investees' human rights policies and processes; management of their respective salient human rights issues; business model red flags that increase the likelihood of human rights harms; and the real-world impacts of the company on people, including the real-world outcomes of their due diligence efforts. Where investment portfolios are especially large, use a "risk-based approach" to identify particularly high-risk sections of the portfolio where the risk of adverse impacts is most significant. Based on this assessment, prioritise investees for further assessment.
- As part of efforts to meaningfully assess the human rights performance of investees and address challenges in the data landscape, consult with relevant stakeholders, such as civil society organisations and trade unions.
- Engage ESG reporting frameworks, benchmarks and data providers to ensure that the research methodologies, corporate performance data and advisory services used to assess investees are aligned with the UNGPs and reflect real-world outcomes for people. Where necessary, commit to supporting the development of new frameworks or better approaches to evaluating human rights performance.
- Engage investees in constructive dialogue to promote: (1) the adoption of human rights policies, governance, due diligence and effective grievance mechanisms and (2) the provision of remedy for victims of human rights abuse where the investee has caused or contributed to adverse human rights impacts.
- Engage portfolio companies to address root causes of short-termism, for example, by:
  - a. Calling for integration of human rights into governance expectations and board committee responsibilities;
  - b. Tying executive pay to corporate human rights performance;
  - c. Asking investee companies for long-term plans and cumulative earnings reporting in which each quarter builds on the next (three months, six months, nine months and then the full year), which leaves in place the transparency of regular reporting while avoiding the quarter-to-quarter comparisons that drive short-term behaviour;
  - d. Elevating stakeholder voice and perspectives in corporate governance and ownership structures, such as by reserving board seats for employees, promoting opportunities for employee ownership and supporting the adoption constituency statutes and reforms of corporate ownership law; and
  - e. Engaging peers whose investment practices pressure boards to prioritise short-term returns over human rights and long-term sustainability.
- In the context of public equities, file and support shareholder proposals that reflect the expectations of the UNGPs. Develop proxy voting guidelines that reflect a commitment to human rights, engage in proxy voting in line with that commitment and publish a proxy voting report.
- Responsibly engage policymakers and standard-setting bodies to tackle systemic human rights risks and create enabling environments for responsible business conduct that is grounded in respect for human rights and access to remedy for affected stakeholders.
- Where the investor is linked to the human rights harm through its investees, use and build the institution's leverage to promote and enable the provision of remedy for victims of business-related human rights abuse, including by recalling the expectation that the investee company have in place an individual operational-level grievance mechanism or by participating in collective platforms in line with the UNGPs' effectiveness criteria.
- Publicly disclose how the institution is addressing salient human rights risks and impacts connected with investment activities.

## Recommendations for other actors in the investment ecosystem

### A. *Investor associations and networks*

- Build internal capacity around rights-respecting investment and offer guidance for members on the investor responsibility to respect human rights, including in relation to: (1) how to reconcile an investor's fiduciary duties and its responsibility to respect human rights; (2) how to identify and prioritise companies for engagement within investment portfolios; and (3) practical case studies of investor due diligence across asset classes.
- Use convening power to share learnings, challenges and good practices among institutional investors, as well as to use collective leverage to influence standard-setting bodies in the direction of alignment with the UNGPs.
- Call for alignment of ESG benchmarks, data providers and reporting frameworks with the UNGPs.
- Set requirements for investor members to implement the UNGPs and hold investor members accountable for underperformance on embedding respect for human rights in investment decisions and stewardship activities, including proxy voting.

### B. *Civil society organisations, academia and research institutions*

- Increase internal capacity on the intersection of investment and human rights, as well as the range of investment tools and actors, such as data service providers and credit rating agencies, in order to enhance the efficacy of stakeholder engagement with the investment industry.
- Gather and communicate data relevant to institutional investors and their human rights commitments and performance, including outcomes for people, in order to facilitate the identification of gaps and good practices and inform investor due diligence.
- Develop practical guidance and tools for investors on rights-respecting investment practices across the full investment lifecycle, as well as across asset classes and investment strategies.
- Collaborate with and support responsible investors to promote respect for human rights in investment portfolios, for example, by directly advising investors on rights-respecting investment, collaborating with investors on developing shareholder proposals and participating in corporate accountability campaigns alongside investors.
- Dedicate increased attention to the investor responsibly to respect human rights, including in terms of accountability under national, regional and international laws.

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# Introduction

Unanimously endorsed by Member States at the UN Human Rights Council in 2011, the Guiding Principles on Business and Human Rights ('Guiding Principles') are the global authoritative standard on the respective roles of State and business enterprises in ensuring business respect for human rights. They established a common global platform for action to advance responsible business conduct, on which cumulative progress could be built.<sup>1</sup> The Guiding Principles are now ten years old—a key milestone as well as an opportunity to learn from the progress and challenges to date and, crucially, make a renewed push for global implementation of the Guiding Principles in the decade ahead.

The 10th anniversary of the Guiding Principles comes at a time of unparalleled challenges and compounding crises—from the COVID-19 pandemic and growing inequalities to the climate crisis, and the myriad risks posed by rapidly evolving digital technologies. A corporate culture of short-termism remains rampant in financial markets, with devastating consequences for people and planet.

Addressing the role of business in this context is essential for meeting these challenges, and institutional investors have a vital role to play. Public debates around the purpose of the corporation reflect this. Calls for a shift away from a singular focus on maximising profits for shareholders to one where companies work in the interest of broader stakeholders, including workers, affected communities and society at large are increasingly common.<sup>2</sup> With this have come more widespread discussions around to whom companies should be accountable and how those who hold the purse strings – particularly institutional investors – should restructure their own ways of doing business to fully take into account stakeholder interests.

The three pillars of the Guiding Principles provide a critical framework for solving these complex global challenges. By providing stakeholders with practical guidance for centring the welfare and dignity of individuals and communities across all aspects of business, including corporate ownership, finance and governance, they also provide a critical tool for those calling for 'stakeholder capitalism.'<sup>3</sup>

The responsibility to respect human rights as set out by the Guiding Principles applies to all investors regardless of size, location, ownership or structure.<sup>4</sup> The Organisation for Economic Co-operation and Development (OECD) elaborated on this responsibility in dedicated guidance for institutional investors in 2017.<sup>5</sup> A number of recent regulatory developments are also translating these expectations into legal requirements.<sup>6</sup> For example, through the Sustainable Finance Disclosure Regulation, the European Union (EU) requires investors to disclose the adverse impacts of their investment decisions on people and planet, independent of financial materiality, and their due diligence in addressing those impacts.<sup>7</sup>

In short, ten years after the endorsement of the Guiding Principles, the expectation that businesses, including investors, respect human rights is increasingly understood as a core expectation for how all business and investment should be done. In its efforts to assess the first decade of Guiding Principles implementation and develop a roadmap for meaningful action in the decade ahead, the UNGPs 10+ project recognises the critical need to shine a brighter light on the role of institutional investors as key to speeding and scaling up business respect for human rights.<sup>8</sup>

## Mandate, scope and methodology

This report is part of UNGPs 10+ project launched in July 2020 by the Working Group on business and transnational corporations and other business enterprises ('Working Group') to take stock of implementation of the Guiding Principles to date and chart a course for increased action by States and businesses in the decade ahead.<sup>9</sup> It focuses on institutional investors and the actors who work with and influence them, including State actors, civil society organisations, data providers and consultants, and is an addendum to the Working Group's 'UNGPs 10+' report to the June 2021 sessions of the Human Rights Council.<sup>10</sup>

A range of submissions<sup>11</sup> and other inputs shared by a diverse range of stakeholders throughout the course of the UNGPs 10+ project inform this report.<sup>12</sup> It also draws from the project's targeted 'investor track' research and dedicated consultations with investors,<sup>13</sup> civil society organisations,<sup>14</sup> and multi-stakeholder audiences,<sup>15</sup> as well as an online survey on investor practice to date.<sup>16</sup>

For the purposes of this report, institutional investors<sup>17</sup> include asset owners (such as public and private pension funds, sovereign wealth funds, endowments, family offices and faith-based organisations) and asset managers (such as stand-alone asset management firms, hedge funds, mutual funds and private sector investment banks and insurance companies in relation to their investment functions). This report also aims

to cover public and private equities, fixed income, real estate, infrastructure, commodities and other types of asset classes and strategies such as multi-asset strategies and funds of funds.

The report targets the core business of asset owners and asset managers, namely, their investment activities. The report touches on investors' operational activities, such as the hiring of in-house human rights expertise and cross-functional training of staff on human rights. However, it does not address the human rights due diligence expectations of investors as employers or in the context of non-investment related business relationships due to the fact that these roles are addressed in an array of existing reports and tools on corporate human rights due diligence.

This report provides a summary of what rights-respecting investment entails, based on the expectations in the Guiding Principles. It outlines how enabling environments have fostered greater investor respect for human rights over the past decade and then summarises signs of progress as well as major gaps and barriers to future progress. It wraps up by providing a set of recommendations for increasing investor action over the course of the next ten years and beyond, concluding that a widespread and serious embrace of long-term thinking and decision-making within investment institutions and the full spectrum of actors they work with is an essential and core component of upholding the dignity and wellbeing of individuals and communities.

### For more information, see:

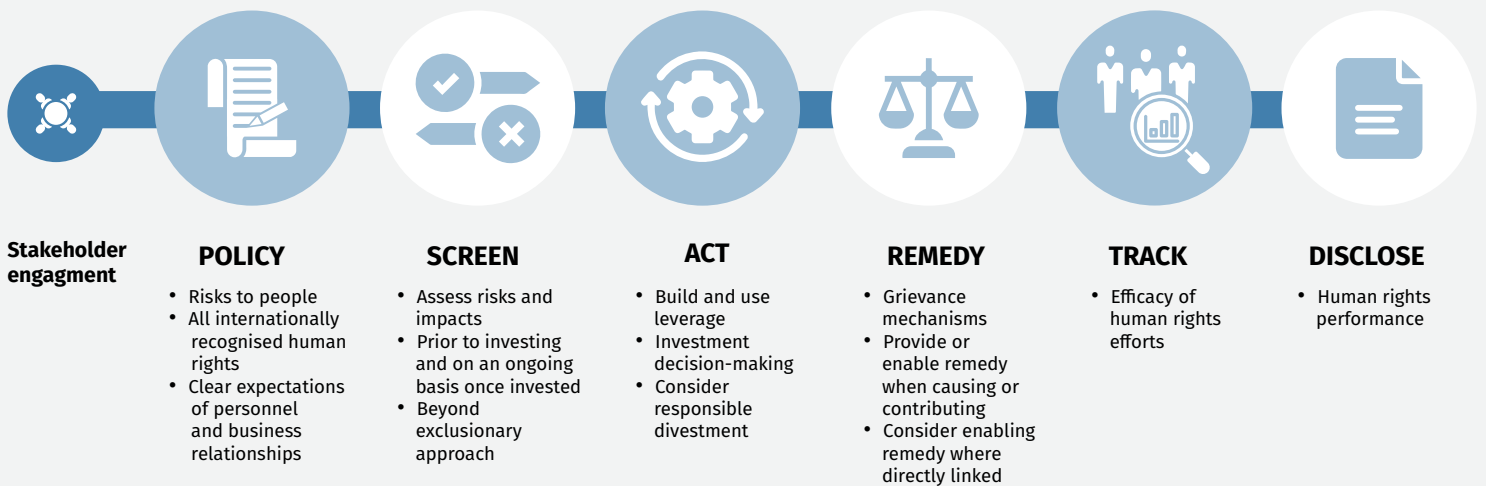
UNGPs 10+ project web page

UNGPs 10+ portal hosted by the Business & Human Rights Resource Centre

Written inputs to UNGPs 10+ with more than 200 submissions from States, business organizations, national human rights institutions trade unions, indigenous peoples, civil society organisations and others



# Rights-respecting investment



While engagement with human rights issues among socially responsible investors has a longstanding history (see section IV), the shift in approach to aligning investment practices with international standards such as the Guiding Principles has only recently begun. This section restates key elements regarding the responsibility of investors to respect human rights.

## Policy commitment and embedding



The Guiding Principles expect institutional investors to have in place a policy commitment to respect all internationally recognised human rights – understood, at a minimum, as those expressed in the International Bill of Rights<sup>18</sup> and

the principles concerning fundamental rights set out in the International Labour Organization’s Declaration on Fundamental Principles and Rights at Work.<sup>19</sup> The policy should be approved at the most senior level of the institution, describe the institution’s human rights expectations of all of its business relationships and be publicly communicated. The policy commitment should also elaborate on how the institution operationalises its human rights commitment through its oversight and governance structures, builds human rights expertise across the institution, embeds human rights criteria throughout the whole of its investment activities and engages with all business partners, including investee companies but also, depending on the investor type, external asset managers, ratings agencies, index fund providers, private equity partners, placement firms, research firms, consultants and other service providers.<sup>20</sup>

### Human rights due diligence

As part of their responsibility to respect human rights, investors are expected to carry out human rights due diligence during the pre-investment phase as well as during the life of their investment in order to know how their investment activities are connected with human rights risks and show how they take steps to address these risks. How this is done in practice will vary across asset classes, investment strategy and where in the investment value chain an investor sits.



#### Assessing human rights risks and adverse impacts

Human right due diligence begins with identifying and assessing real and potential adverse human rights impacts across investment activities and business relationships, including investees.<sup>21</sup> This risk-based approach is based on assessing risks to people, not to financial returns, and priority for action should be based on where the risk of adverse impacts on people are most severe (as a function of its scale, scope and irremediable character). Based on this risk assessment, investors should address their adverse human rights impacts, recognising that it may not always be possible to address them simultaneously. Therefore, investors are expected to first prioritise high-risk products, services and business relationships that are actually or likely to be associated with more severe risks for further assessment and due diligence.<sup>22</sup>

This approach differs from traditional exclusionary or negative screens used by many responsible investors to identify and remove severe human rights risks in a company's operations and value chains from their investment portfolios. Through negative screens that focus on sectors or operating contexts, investors are able to exclude certain securities from their investments based on social or environmental criteria, including human rights concerns. Typical investor screens include tobacco, alcohol, controversial weapons and fossil fuels. However, while screening companies in sectors with known severe human rights risks or for

companies operating in high-risk contexts may help ensure portfolios are free from some severe impacts, companies of all sectors and sizes and in any operating context may be connected to human rights abuses.<sup>23</sup> For instance, renewable energy projects have been linked to numerous and severe human rights abuses, including 'killings, threats and intimidation; land grabs; dangerous working conditions and poverty wages and harm to indigenous peoples' lives and livelihoods.<sup>24</sup>

Investor assessment processes, including during investment decision-making and when prioritising investees for engagement, should therefore go beyond traditional exclusionary approaches to include assessment of: an existing or potential investees' human rights policies and due diligence processes, including as these relate to the management of severe (or salient) and geographic



Refer to the OECD's guidance on Responsible Business Conduct for Institutional Investors for approaches to identifying and assessing real and potential adverse impacts by asset class and investment strategy.

risks, business model red flags<sup>25</sup> and the real-world impacts of a company on people, including the outcomes of their due diligence efforts.

#### Acting on human rights risk and adverse impacts

In order to prevent and mitigate adverse human rights impacts connected to investment activities, investors are expected to take appropriate action based on assessment findings. Determining what action is most appropriate depends on how the investor is connected to the human rights risk or impact, which can take three forms. As highlighted, for example, by the PRI, there are impacts that an investor: '(1) has caused – through its own business activities (e.g., [impacts on] its own employees)

[or] where its own activities remove or reduce someone's ability to enjoy a human right [such as] where the investor holds a controlling stake in an investee company (e.g., through the majority ownership model in private equity)... (2) has contributed to – a) through its own business activities where it is one of several contributors or b) through a business relationship or investment activity that induces or facilitates an outcome from an investee company or project [such as] when the investor holds high ownership stakes and could or should have known about harm, but preventive actions were insufficient; or (3) is directly linked to – through the activities, products or services of an investee company or project.<sup>26</sup>

Investors should therefore assess where on the spectrum of cause, contribution and linkage they sit in relation to human rights harm and take action accordingly. As noted by Professor John Ruggie, the author of the Guiding Principles, 'There is a continuum between contribution and linkage. A variety of factors can determine where on that continuum a particular instance may sit [including] the extent to which a business enabled, encouraged, or motivated human rights harm by another; the extent to which it could or should have known about such harm; and the quality of any mitigating steps it has taken to address it.'<sup>27</sup>

Where an investor has caused harm, they are expected to cease or prevent the action causing the harm and play a direct role in remediating the harm. Where an investor has contributed to harm, they are expected to cease or prevent the action contributing to the harm, play a direct role in remediating the harm to the extent that they have contributed to it and build and use their leverage to influence other actors contributing to the harm to prevent, mitigate and address the harm. Where investors are directly linked to negative human rights impacts through their investment activities, they are expected to build and use their leverage to influence other actors causing or contributing to the harm to prevent, mitigate and address the harm.<sup>28</sup> While investors are not expected to play a direct role in remediating the harm in cases of linkage, they should seek to build and use their leverage to

**Where investors are directly linked to negative human rights impacts through their investment activities, they are expected to build and use their leverage to influence other actors causing or contributing to the harm to prevent, mitigate and address the harm.**

enable remedy for affected rights-holders.<sup>29</sup>

Leverage refers to the 'ability of the business enterprise to effect change in the wrongful practice that is causing or contributing to an adverse human rights impacts.'<sup>30</sup> Forms of investor leverage include engaging companies in dialogue, filing shareholder resolutions, proxy voting, participating in peer-to-peer and multi-stakeholder initiatives, engaging with State institutions and other standard-setting bodies, engaging with other stakeholders such as civil society organisations and integrating human rights criteria into agreements with business relationships, such as Limited Partnership Agreements in the case of private equity.<sup>31</sup> In the case of large passive asset managers, also known as 'universal owners',<sup>32</sup> using leverage to promote public policy that tackles systemic risks to human rights is an especially crucial form of leverage.<sup>33</sup> By effectively owning a slice of the whole economy, universal owners are uniquely exposed to and have a responsibility to address the systemic and collective adverse impacts of the economy as a whole.

An investor's ability to exercise its leverage effectively may be affected by a number of factors. For example, even the largest institutional



investors may be only small minority shareholders in many companies. In the case of publicly traded companies, corporate ownership structures and corporate governance rules and practices in some countries may impede minority shareholders from exercising leverage. Certain asset classes may also limit some forms of investor leverage, such as investors in corporate or government bonds who may have very limited opportunities to influence the bond issuer, as in the case of individual bondholder's influence over a government. However, while the tools and strategies available to different types of investors and investments across asset classes or strategies vary, at times significantly, the underlying responsibility to respect human rights remains the same.

Where an investor lacks sufficient leverage to affect change in the behaviour of an investee company and is unable to increase its leverage, it may consider responsible divestment (or exclusion).<sup>34</sup> The Guiding Principles clarify that a business relationship may have to be terminated if efforts to exercise leverage aimed at addressing an adverse human rights impact prove unsuccessful. As noted for example by the OECD, divestment from a company may be an appropriate response after continuous failed attempts at mitigating the harm, where mitigation is unfeasible or because the severity of the adverse impact warrants it. When considering whether to divest, investors should also assess whether ending the relationship with the investee would result in adverse impacts. Divestment may not be appropriate in all cases because without investors engaging on human rights concerns, there is often no other voice persuading the company to change its practices.<sup>35</sup> As the Guiding Principles make clear, the more severe the abuse, the more quickly the enterprise will need to see change. The Investor Toolkit on Human Rights adds, 'Those who divest from a company are advised to issue a press release explaining why, thereby imposing greater pressure on the company and creating leverage for others who have not divested. This can take place either before or after divestment has been completed.'<sup>36</sup>

### ***Tracking progress and disclosure of own human rights performance***

Like investee companies, investors are expected to track the efficacy of their efforts on an ongoing basis, adapting other elements of their due diligence processes and practices in response to lessons learned based on that tracking. Investors should also publicly disclose their human rights efforts, not only in relation to transactional due diligence at the pre-investment stage, but throughout each stage of the investment lifecycle and across their full investment portfolios. Investor human rights reporting is also a key public good in holding investors accountable for how they manage risks to people in connection with their investment activities, and, as elaborated on below, investors are increasingly required to disclose human rights information.

### **Providing and enabling remedy when harm occurs**



The Guiding Principles clarify that victims of adverse corporate human rights impacts have a right to effective remedy. At the institutional level, investors should have in place their own effective grievance mechanism(s) to support the provision of remedy when they cause or contribute to a situation where someone's human rights are adversely impacted. Where adverse impacts have occurred that the investor has not caused or contributed to, but which are directly linked to its operations, products or services by a business relationship, the responsibility to respect human rights does not require that the investor provide for remediation, though it may take a role in doing so.<sup>37</sup>

The concept of enabling remedy when investment activities are connected to actual or potential human rights harms has yet to be meaningfully explored in the institutional investment space. While investors should consider having systems and processes in place at the institutional level that support civil society, trade unions and others affected by investees in raising concerns about investee conduct, such mechanisms on their own

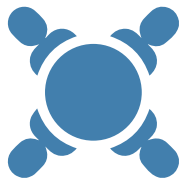
are unlikely to address the need for remedy when harm occurs.<sup>38</sup> Adopting a ‘remedy ecosystem’ approach may help strengthen the ability of investors to enable remedy by:

(1) proactively supporting preparedness for remedy before harm occurs by building and using leverage to communicate expectations on remedy to investees and engage investees on the effectiveness of their grievance mechanisms and

(2) reactively building and using leverage when a harm has occurred to influence those causing or contributing to the harm to focus on remedy, engage with affected rights-holders and other relevant stakeholders and ensure that there is an effective process and meaningful outcome in the provision of remedy.<sup>39</sup>



### Investor-stakeholder engagement



Stakeholders engagement is one of the key features of the Guiding Principles, ranging from gauging human risks to providing or enabling remedies. In the context of the Guiding Principles, key stakeholders should be understood as actually or potentially affected rights-holders, their legitimate representatives and expert organisations.

Investors should always assess companies’ policies and practices regarding stakeholder engagement and on the effectiveness of their grievance mechanisms and use their leverage to promote meaningful stakeholder engagement by investee companies. Investors should also be prepared to directly engage with stakeholders who raise concerns with the institution regarding its investments.

Where investors cause or contribute to negative human rights risks and impacts, including through their investment activities, they should seek to directly engage with actually or potentially affected individuals and communities. In practice, institutional investors are more likely to be connected to negative risks and impacts through direct linkage. In these situations, it may often be impractical for investors to directly engage with adversely impacted rights-holders. In these instances, in addition to trying to engage impacted stakeholders, investors should seek to engage with human rights organisations, experts and credible representatives of rights-holders, such as global trade unions, to inform institutional understanding and prioritisation of human rights risks involved with investment activities and recommended actions to address gaps.

The Working Group has elaborated criteria for effective stakeholder engagement that is integral to robust human rights due diligence. This includes engaging with and enabling critical voices to raise concerns, engaging directly with affected stakeholders in good faith, taking into account the specific risks affecting different groups, including integrating a gender-sensitive approach and collaborating with NGOs and unions in formal partnerships to identify and address potential and actual impacts.<sup>40</sup>

### Investment at the State-business nexus

The responsibility of business to respect human rights applies to all enterprises regardless of their ownership. Thus, the Guiding Principles apply equally to investment entities such as public pension funds, sovereign wealth funds and development finance institutions who are responsible for respecting human rights like any other business enterprise.

Their public nature means that they may bear additional duties under pillar I of the Guiding Principles. Regardless, where the State is operating as an investor and/or is the statutory authority of an investment institution, it must seek to uphold its human rights obligations, including by carrying out its own human rights due diligence in connection with its investment activities and, where appropriate, require human rights due diligence by investment entities or projects under their authority or receiving their support.<sup>41</sup> For example, the legislative branch of government plays a key role in developing a legal framework that reflects the human rights expectations of sovereign wealth funds while the executive branch, for example, through ministries of finance, set the mandate for sovereign wealth funds to operate in line with the investor responsibly to respect human rights.

The Working Group has stressed the importance of building on the OECD Guidelines on Corporate Governance of State-Owned Enterprises and the G20/OECD Principles of Corporate Governance to enhance the governance and management of the human rights impacts of State-owned enterprises, including those related to investment. These instruments are closely related to existing guidance on responsible business conduct and human rights, in particular the OECD Guidelines for Multinational Enterprises and the UN Guiding Principles on Business and Human Rights.<sup>42</sup>







# The enabling environment for rights-respecting investment

Progress in investor uptake of the Guiding Principles over the past decade has been bolstered if not driven by increased efforts from standard-setting bodies to create an enabling environment for rights-respecting investment. PRI's Regulation Database documents the last decade's rise in sustainable finance policies and regulations around the world, including those related to human rights.<sup>43</sup> These initiatives from a multitude of different actors – including governments, multilateral organisations, reporting frameworks, industry associations, multi-stakeholder platforms and stock exchanges – play a critical role in driving Guiding Principles implementation at scale and facilitating a level playing field for investors.

## **Mandatory measures are accelerating progress toward rights-respecting investment**

The European Union (EU) has taken on a leadership role in redefining the responsibilities of institutional investors by ensuring that ESG considerations, including human rights, are at the heart of the region's financial system. With the aim of better informing sustainable investment, the EU Non-Financial Reporting Directive (NFRD), first introduced in 2014, calls on companies to report on their due diligence policies and processes for managing environmental and social risk in line with the OECD Guidelines.<sup>44</sup> The NFRD is currently being revised in response to proposals for strengthening the directive's due diligence reporting expectations.<sup>45</sup> Through the Sustainable Finance Disclosure Regulation, applicable as of March 2021, European investors are also now required to disclose the adverse impacts of their investment decisions on people and planet, independent of financial materiality, and their due diligence in addressing those impacts, in line with international standards.<sup>46</sup> This requirement applies to all investment advisors who sell products in Europe and thus covers all large investment advisers worldwide. Moreover, the minimum safeguards under the EU Taxonomy,

which sets environmental performance thresholds in relation to new legal disclosure obligations for European financial market participants, are based on internationally recognised human rights and specifically require alignment with the Guiding Principles.<sup>47</sup> While not yet finalised, the EU directive on mandatory human rights and environmental due diligence is envisioned to include coverage of the financial sector and is driving investor and investee attention toward their own human rights responsibilities while also helping to bridge long-standing siloes when it comes to corporate action on people and planet.<sup>48</sup>

At the national level, the Modern Slavery Acts in the United Kingdom and Australia require certain large entities, including investors, based or operating in the respective jurisdictions, to report annually on their modern slavery due diligence.<sup>49</sup> France's comprehensive duty of vigilance law also covers certain institutional investors in requiring certain companies to conduct and be accountable for their human rights due diligence policies, processes and practices.<sup>50</sup>

## **The 'business case' is bolstering investor uptake**

Investors increasingly recognise fiduciary duties to address longer-term risks such as human rights risks in investments.<sup>51</sup> Over the past decade, a wide range of research has documented the correlation between human rights risks, corporate financial performance and risks to investment.<sup>52</sup> Socially responsible companies are perceived as less risky by investors and lenders, and companies who address their social and environmental impacts enjoy lower risk premia, placing them in a better position for raising new capital.<sup>53</sup> For example, in May 2020, investors representing over \$5 trillion in assets under management stated that 'where there are the most severe (i.e. salient) risks to human rights, there are material risks to business.'<sup>54</sup> In turn, the business benefits are projected to only

increase as ESG investing may 'get a considerable boost from a substantial intergenerational wealth transfer, from baby-boomer parents to millennials.<sup>55</sup>

A number of initiatives have also emerged in the past ten years to help further clarify the relationship between severe human rights risks in investment portfolios and material costs. For example, the Sustainability Accounting Standards Board (SASB) Materiality Map identifies a number of human rights risks that are deemed to likely affect the financial condition or operating performance of business. Moreover, in March 2021, as part of its engagement with SASB's human capital management project, Rights CoLab announced it teamed up with the Data for Good Scholars (DfG) Program of Columbia University's Data Science Institute to identify new relationships between labour-related human rights risks and financial materiality.<sup>56</sup> SASB is now backed by investors with more than US\$41 trillion Assets Under Management (AUM), and the largest institutional investors with universal ownership are increasingly demanding that investee companies disclose against the SASB standards.<sup>57</sup> Shareholder resolutions that have requested material disclosures compliant with SASB standards have fared especially well.

First Peoples Worldwide has also documented the material costs for investors where companies fail to act with due diligence to respect the rights of Indigenous Peoples, finding that firms with ownership stake in the Dakota Access Pipeline project incurred no less than US\$7.5 billion in costs.<sup>58</sup> Moreover, a study published in 2020 found that firms associated with the assassination of civil society activists involved in mining activity have large, negative abnormal returns following the event.<sup>59</sup>



While not exclusively about human rights risks, Harvard's Belfer Center has also demonstrated a link between start-up technology companies that fail and bad performance in addressing ESG risks, including risks associated with product integrity, stakeholder management and governance. These early stage companies often experience ESG risk-linked failures at an advanced stage of the venture after private equity investors have made significant investments in a company.<sup>60</sup> The costs associated with how well companies manage human rights risks persist when private companies reach maturity and go public. For example, the Uber and Lyft IPOs saw significant losses in valuation due to human rights issues involving their business models, working conditions and governance.<sup>61</sup>

### **Institutional uptake is helping to promote rights-respecting investment**

Various multilateral institutions over the past decade have addressed investor respect for human rights and, in some cases, have provided necessary guidance to help further the uptake of the Guiding Principles. In addition to the aforementioned OECD guidance for institutional investors,<sup>62</sup> the UN Environment Programme Finance Initiative in 2014 revised its Human Rights Guidance Tool for the Financial Sector, including investors,<sup>63</sup> UNICEF published Investor Guidance on Integrating Children's Rights into Investment Decision-Making alongside Sustainalytics in 2019,<sup>64</sup> and the UN OHCHR B-Tech Project released guidance on rights-respecting investment in digital technology companies in 2021.<sup>65</sup> Moreover, the Impact Standards for Private Equity Funds set out the expectation that fund-level managers, in the context of impact investing, respect human rights in line with the Guiding Principles and provide effective grievance redress mechanisms as a means of demonstrating appropriate governance controls.<sup>66</sup> UN special mandate holders have, in some cases, directly spoken to the role of investors in preventing, mitigating and addressing adverse impacts on human rights.<sup>67</sup>

### **Industry initiatives and associations are responding to calls for support**

A number of investor initiatives and associations have emerged to support rights-respecting

investment practices. The Investor Alliance for Human Rights, launched in 2018 as an initiative of the Interfaith Center on Corporate Responsibility (ICCR), seeks to provide a collective action platform for responsible investment that is grounded in respect for human rights.<sup>68</sup> The Investor Alliance, whose membership has grown to represent over US\$5 trillion AUM, published the Investor Toolkit on Human Rights, which provides practical guidance and tools to support investor uptake of the Guiding Principles.<sup>69</sup> In addition, the UN-supported Principles for Responsible Investment (PRI) – which supports over 3,000 signatory investors representing more than US\$103 trillion AUM – issued a human rights framework in 2020, outlining a multi-year agenda to work towards respect for human rights across the financial system and a commitment to increase accountability among investor signatories by introducing human rights questions into the PRI Reporting Framework.<sup>70</sup> Sustainable Investment Forums (SIFs) are also playing an increasing role in promoting investor respect for human rights, such as Dansif’s partnership with the Danish Institute for Human Rights to build the capacity of ESG professionals on human rights<sup>71</sup> and Eurosif’s input into the EU process toward a mandatory human rights and environmental due diligence directive.<sup>72</sup> At the same time, investors continue to express the need for greater guidance and expertise when it comes to practical implementation of the investor responsibility to respect human rights under the Guiding Principles.

### Some stock exchanges are encouraging public company disclosure on human rights

In some cases, stock exchanges have played a role in informing investors about human rights risks.<sup>73</sup> An analysis of human rights references in stock exchange ESG disclosure guidance carried out by the Sustainable Stock Exchanges Initiative found that most stock exchanges (48 out of 56) mention human rights in their ESG disclosure guidance but only 16 out of 56 stock exchanges refer explicitly to the Guiding Principles.<sup>74</sup> In addition, the Long-Term Stock Exchange, an SEC-registered national securities exchange built to serve companies and investors who share a long-term vision, provides a model of securities trading that are more conducive to rights-respecting investment practices.<sup>75</sup>

### Despite progress, policy coherence remains a challenge

While there has been progress in recent years, uptake of the Guiding Principles among governments and standard-setting bodies has been inconsistent and insufficient. For example, there is widespread misalignment between legal frameworks for investment decision-making and the Guiding Principles, as well as weak enforcement of existing environmental and social requirements where these exist.<sup>76</sup> Furthermore, investors have cited that the variation of legal standards between and within countries and regions regarding corporate human rights due diligence contributes to the limited availability of consistent disclosures and data from investee companies. Furthermore, while national action plans on business and human rights are important avenues to increase coherence across state institutions, very few plans refer to the roles and responsibilities of asset owners and managers in particular. Where institutional investors are mentioned, listed actions are descriptive of what already exists without commitments to future work.<sup>77</sup>

Moreover, there remains a capacity gap within multilateral entities, including the United Nations, when it comes to speaking out about investor responsibility and accountability in relation to human rights. In addition, while some development banks have adopted human rights commitments,<sup>78</sup> such commitments have yet to be embedded into the investment functions of banks.





# Progress and gaps in investor uptake

Individually and through coordinated platforms, investors such as pension funds and faith-based groups have engaged companies on issues related to human rights since the early 1970s. These efforts have touched on a wide range of topics, from anti-apartheid efforts in South Africa to climate change and fossil fuel divestment to forced labour in global supply chains.

The last five years in particular have seen exponential growth in ESG-based investing, rising to US\$40.5 trillion of global AUM in 2020<sup>79</sup> and accounting for over 40 percent of total AUM worldwide.<sup>80</sup> Impact investing, which aims to generate positive social and environmental impacts alongside financial returns, was estimated in 2020 to include over 1,720 organisations managing US\$715 billion.<sup>81</sup> And investors have been increasingly mobilised to help meet the estimated financing gap of US\$2.5-3 trillion per year to achieve the 2030 Agenda's Sustainable Development Goals (SDGs) in developing countries, not least in part due to the fact that the achievement of the SDGs could open up US\$12 trillion in market opportunities.<sup>82</sup>

Despite the trend toward increased ESG investing, human rights are still rarely addressed in a systematic or principled way. The vast majority of institutional investors have yet to meaningfully engage with their human rights responsibilities. Human rights are often seen as a narrow set of issues limited to the 'S' of ESG rather than understood as relevant across a wide range of ESG-related issues. Even areas of investor activity where consideration of social impacts are seemingly embedded have been largely detached from efforts to align investment activities with the expectations laid out by the Guiding Principles. This includes in the context of impact investing<sup>83</sup> and investing toward achievement of the SDGs.<sup>84</sup>

Confirming this challenge, a 2018 Working Group report to the United Nations General Assembly found

that although more investors were scrutinising and pressuring companies to manage human rights risks and prevent abuses, most are failing to live up to their human rights responsibilities.<sup>85</sup> The Working Group called for investors to 'implement human rights due diligence as part of their own responsibility under the Guiding Principles, more systematically require effective human rights due diligence by the companies they invest in, and coordinate with other organisations and platforms to ensure alignment and meaningful engagement with companies.'<sup>86</sup>

The following section outlines key progress and gaps in uptake to meet the investor responsibility to respect human rights to date.

## Short-termism signals misalignment with human rights responsibilities

The misalignment between most institutional investment practices and the expectations laid out by the Guiding Principles is apparent in the long-prevalent culture of corporate short-termism in financial markets. Shareholder pay-outs and compensation for executives and directors within many companies have been accompanied by cost-cutting and wage stagnation for the rest.<sup>87</sup> As pointed out by Professor John Ruggie, an underlying factor of this trend is investor pressure, especially from hedge funds, certain types of activist investors and private equity firms, whose central goal is obtaining short-term financial returns and moving on.<sup>88</sup> For example, in March 2021, the chairman and CEO of Danone stepped down under pressure from activist investors prioritising short-term shareholder returns over ESG commitments.<sup>89</sup> Yet, Professor Ruggie adds that 'even union pension funds, university endowments and sovereign wealth funds have sought higher returns in riskier and shorter-term investments in order to meet their commitments to current and soon-to-be beneficiaries.'<sup>90</sup>

One way in which the drive for short-term profits over long-term sustainability is operationalised is through executive pay packages that are tied to short-term share-price moves,<sup>91</sup> and the associated push to demonstrate positive results in quarterly earnings reports. A 2020 study found that just 604 companies in the Russell 3000 index, which benchmarks the 3,000 largest publicly held companies in U.S. stock market, tied compensation to any kind of ESG target,<sup>92</sup> most of which are related to climate and none to human rights. One challenge expressed by responsible investors involves how to define and measure sustainable practices,<sup>93</sup> a further indication that human rights standards have yet to permeate investors' understanding of long-term sustainable business. In some cases, investors have even worked to undermine the adoption of constituency statutes, which would require corporate directors to consider non-shareholder interests when making business decisions.<sup>94</sup>

Another factor is that human rights considerations are also often seen as secondary to or inconsistent with investors' fiduciary duty. While there are exceptions among certain public pension funds<sup>95</sup> and there is movement to address this in the United Kingdom<sup>96</sup> and in Europe,<sup>97</sup> there are still barriers stemming from the potential misinterpretation of fiduciary duties as limiting the ability of investors to devote assets and efforts to anything that does not increase the financial standing of pension plan beneficiaries or customers in the short-term.

The human costs of short-termism and incentives that drive cost cutting are apparent in, for example, the healthcare sector. A 2021 economic analysis of private equity (PE) ownership of nursing homes in the United States found that "PE ownership increases the short-term mortality of Medicare patients by 10%, implying 20,150 lives lost due to PE ownership over [a] twelve-year sample period." The study found that declines in nursing staff and compliance with standards help to explain these effects.<sup>98</sup>



### **Most investors continue to have significant capacity challenges**

Knowledge of human rights, including how human rights are defined, how they are relevant across ESG factors and what meaningful human rights due diligence looks like, remains limited throughout the institutional investor community. The Guiding Principles make clear that appropriate business and human rights expertise is essential for informing and implementing human rights policy commitments and due diligence.<sup>99</sup> Yet few institutions have in-house expertise or consult with business and human rights experts, and instead rely on individuals with expertise in ESG, sustainability, corporate social responsibility or environmental risk management to lead work on human rights.

This barrier for right-respecting investment is compounded by the absence of industry-wide ESG standards, let alone ones that align with human rights, and the relatively limited amount of guidance and resources on human rights tailored to the daily realities of the investor community. The venture capital community in particular has limited tools and data available to systematically evaluate and manage its human rights and broader ESG risks.<sup>100</sup>

As a result, human rights are often misunderstood by investors as 'niche,' covering a relatively narrow set of issues. For example, some investors may regard issues involving Indigenous Peoples or forced labour in the supply chain as relating to human rights while failing to recognise workplace diversity and inclusion, occupational health and safety and data privacy as human rights issues. Human rights are also often seen as limited to the 'S' of ESG rather than understood as relevant across



a wide range of ESG-related concerns, such as climate change, environmental harm and corporate lobbying. Similarly, human rights may only be considered relevant to certain parts of a business, such as in the supply chain or community impacts, rather than in own operations and throughout the entire value chain.

While in some instances investors may engage companies on their human rights policy commitments, due diligence and grievance mechanisms, these are rarely assessed for quality and effectiveness as sufficient human rights expertise for evaluation and analysis remains limited across most investment firms.

### **Investor human rights commitments exist but remain limited**

A number of asset owners and managers engage companies on human rights issues, yet very few have in place robust, institution-wide policy commitments and governance structures to respect human rights in line with the Guiding Principles. In 2020, 75 of the world's largest asset managers were assessed on their human rights performance. Few were found to have in place specific human rights policy commitments, including commitments to influence corporate behaviour on severe human rights impacts.<sup>101</sup> Where public and private equity investors have responsible investment policies in place, these are often framed around ESG and sustainability, with only occasional reference to specific human rights issues, as opposed to a robust commitment to respect all internationally recognised human rights and conduct human rights due diligence.

Rising attention to and resources focused on the investor responsibility to respect human rights in recent years have contributed to some investors acknowledging their human rights responsibilities. For example, in 2020 by a public statement, investors with over US\$5 trillion AUM recognised their own responsibilities to respect human rights under the Guiding Principles.<sup>102</sup>

While still rare, some investors have also started adopting stand-alone human rights

policy commitments or integrated human rights commitments into investment or engagement policies. For example, in 2021, Sycomore Asset Management adopted a human rights policy in which the firm commits to carrying out human rights due diligence, prioritising action based on and assessment of the most severe impacts on people and providing, cooperating in or enabling remedy when involved in adverse human rights impacts.<sup>103</sup> In March 2021, BlackRock, the world's largest asset manager, publicly communicated its commitment to engaging companies on human rights and asked that 'companies report on how they integrate human rights considerations into their operations and risk management processes and demonstrate the steps they are taking to address these issues.'<sup>104</sup> Some investors have also listed the main industries represented in their holdings alongside the salient issues present in that industry, such as NEI Investments in Canada, whose policy highlights the right to free, prior and informed consent (FPIC) of Indigenous Peoples as a sector-wide salient risk in the extractives industry.<sup>105</sup>

Some public funds have also committed to human rights and have sought to embed this commitment by training employees and communicating their human rights expectations of boards of directors to investee companies and other business relationships.<sup>106</sup> For instance, Norges Bank Investment Management (NBIM)<sup>107</sup> has publicly disclosed how its investment-level human rights commitments translate into the institution's expectations for companies. Reflecting a sector-focused approach, the Council on Ethics of the Swedish national pension funds published investor expectations on respect for human rights by technology companies.<sup>108</sup>

### **Progress on screening for human rights risks, yet the data dilemma persists**

A 2020 study found that large asset managers lack sufficient due diligence processes to appropriately identify salient negative human rights impacts. Only nine percent of asset managers evaluated were able to identify negative impacts that may be a result of their investments.<sup>109</sup> A 2018 study found that pension fund managers struggle to

implement human rights policies and procedures to consistently predict, detect and resolve human rights issues, particularly in the context of infrastructure investments.<sup>110</sup> While some pension funds have made greater strides than others, even the most advanced funds struggle to systematise and mainstream their risk assessment procedures. A further complication for pension funds is that they often do not select their own investments, but rather outsource these decisions to external investment managers. Also, some socially responsible investors rely on negative screens to exclude severe risks associated with companies in certain industries or operating contexts while failing to meaningfully assess investees in other industries or operating contexts for severe risks.

While there is no empirical data specifically analysing the uptake of the Guiding Principles among private equity firms and venture capital funds, a 2019 Harvard study found that venture capital in particular lags behind investors in other asset classes on ESG, demonstrating no systematic approach to assessing and managing ESG risks.<sup>111</sup> Significant gaps also remain in the fixed income space, as current practices do not adequately assess or account for the human rights implications of social bonds, which are debt securities sold to investors whose proceeds are used to finance projects with a defined social benefit such as affordable housing, education, food security and access to healthcare.<sup>112</sup> Moreover, very few investors consider the States' human rights policies and practices when assessing whether to invest in government bonds such as sovereign wealth bonds.<sup>113</sup>

The ability of investors to meaningfully assess and prioritise human rights risks connected with their investment activities has been starkly challenged by the fact that meaningful corporate human rights disclosure has been the exception, not the norm, over the past decade. Measuring human rights performance and outcomes is also difficult for many investors due to the often-qualitative nature of human rights-related data. Where investors have

portfolios that include thousands of companies, assessing human rights risks at scale is also uniquely challenging.

A root cause of these challenges has been the inconsistent integration of the Guiding Principles process framework across the myriad reporting frameworks, benchmarks and other data and research products used by investors to assess companies.<sup>114</sup> Moreover, because of general aggregation of ratings across individual ESG factors, companies that contribute to human rights harms may be deemed strong performers on ESG overall due to their high rankings on environmental criteria, despite, for example, discriminating against employees based on gender identity or systematically breaching user privacy. For example, ESG funds with heavy exposure to technology companies have outperformed traditional funds during the COVID-19 crisis,<sup>115</sup> yet multiple sources have attributed this improved financial performance to the funds' low exposure to energy-sector companies.

In response to these challenges, an investor coalition led by Boston Common Asset Management and representing nearly US\$4 trillion AUM was founded in 2015. The coalition endorses the UN Guiding Principles Reporting Framework as a key tool for incentivising 'improved disclosure and enabling investors to review companies' understanding and management of human rights risks.<sup>116</sup> This was followed by APG, Aviva and Nordea, who along with other partners, co-founded the Corporate Human Rights Benchmark in 2017.<sup>117</sup> A number of key tools have also emerged in recent years for investors to use in assessing corporate respect for human rights to inform their own human rights due diligence.

### Tools and benchmarks using the Guiding Principles

- The Corporate Human Rights Benchmark assesses the human rights disclosure of 230 global companies in the agricultural products, apparel, extractives, information and communications technology (ICT) manufacturing and automotive manufacturing sectors.
- The World Benchmarking Alliance's social transformation framework assesses 2,000 companies across 30+ sectors, including the financial sector, on a common set of indicators based on the CHRB.<sup>118</sup>
- The UN Guiding Principles Reporting Framework Database contains information on corporate human rights disclosures.<sup>119</sup>
- KnowTheChain evaluates companies on forced labour policies and due diligence practices.<sup>120</sup>
- Ranking Digital Rights Corporate Accountability Index measures ICT companies' performance on privacy and freedom of expression.<sup>121</sup>
- BankTrack's Human Rights Benchmark assesses human rights due diligence by banks.<sup>122</sup>
- The Renewable Energy and Human Rights benchmarks the human rights performance of the largest renewable energy companies.<sup>123</sup>
- Behind the Barcodes and Behind the Brands evaluate supermarkets and food companies, respectively.<sup>124</sup>
- The Access to Medicine Index assesses the pharmaceutical industry on its human rights practices.<sup>125</sup>
- The Transition Minerals Tracker provides data on the companies that produce the minerals vital to the renewable energy and electric vehicles sectors.<sup>126</sup>
- The Workforce Disclosure Initiative evaluates decent work and human rights in the workplace from 141 global companies.<sup>127</sup>
- The Responsible Mining Index assesses policies and practices of 38 large-scale mining companies that operate in more than 780 mine sites.<sup>128</sup>
- Shift's Valuing Respect Project's Business Model Red Flags helps investors assess portfolios for human rights risks.<sup>129</sup>
- The Business & Human Rights Resource Centre's website contains information on the human rights impacts of over 9,000 companies.<sup>130</sup>
- Updates to the Global Reporting Initiative (GRI) framework<sup>131</sup> and the S&P Global Corporate Sustainability Assessment (CSA)<sup>132</sup> are also promising developments that may help facilitate further alignment across diverse data sets with the Guiding Principles.



While advocacy by investors, investees and others for standardisation has resulted in some convergence in sustainability frameworks over the past few years, much of this convergence has moved in the direction of focusing on financial materiality metrics, running the risk of continued misalignment with the Guiding Principles.<sup>133</sup>

A fundamental barrier contributing to this challenging landscape is limited data availability on the real-world impacts of business activities and due diligence efforts. Investors and those that work with them have cited that the vast majority of currently available data on human rights performance focuses on input, activities and outputs, and company reporting rarely focuses on actual outcomes for people or the effectiveness of due diligence measures.<sup>134</sup> Public investment funds in particular have stressed that a lack of reliable data that consistently speaks to human rights outcomes is one of the greatest challenges in implementing respect for human rights through

**A fundamental barrier contributing to this challenging landscape is limited data availability on the real-world impacts of business activities and due diligence efforts.**

their investments.<sup>135</sup> Without the ability to confidently measure which investor and investee actions are most effective and when, investors remain unable to confidently and consistently prioritise issues and design appropriate actions. Such data challenges may also have consequences for the effective implementation of regulatory requirements, such as the safeguards clause under the EU taxonomy.<sup>136</sup>

These limitations notwithstanding, the findings of existing assessment frameworks and benchmarks that are based on key concepts of the Guiding Principles remain an important proxy for corporate human rights performance. They provide investors with an indication as to which companies are not demonstrating sufficient input, activity and output that might signal good performance, which should be sufficient to justify increased investor action. Companies that score poorly on these criteria fail to even signal good practices, let alone satisfactory outcomes. A growing number of responsible investors realise this and have started using these tools in their efforts to assess and engage companies.

In the case of sovereign bonds, the data challenge is somewhat different. Tailored guidance and resources for evaluating the human rights track record of States remains extremely limited.<sup>137</sup> In Europe, FIDH (the International Federation for Human Rights) has released States under the Spotlight, which provides non-financial rating of 27 EU Member States and the United Kingdom.<sup>138</sup> While similar tools do not exist for other regions, monitoring and publicly evaluating the human rights performance of States is a core function of human rights systems at the global, regional and national levels. For example, the international human rights system, including UN treaty bodies,<sup>139</sup> Special Procedure mandate holders,<sup>140</sup> independent investigations,<sup>141</sup> and the Universal Periodic Review process<sup>142</sup> all provide country-specific human rights data for investors to consider. At the country level, national human rights institutions play a crucial role in monitoring and publicly reporting on the implementation of international human rights standards.<sup>143</sup>

**Investors increasingly use leverage with companies, yet gaps remain**

To embed respect for human rights throughout the stewardship stage of the investment lifecycle, investors should use and maximise their leverage to facilitate and incentivise respect for human rights.

A key area of progress over the past decade has been the growth of peer-to-peer engagement among public equity investors focused on promoting the uptake of the Guiding Principles among companies. Between 2015 and 2020, approximately 115 institutional investors had engaged with 100 companies through PRI-led collaborative engagements to improve human rights practices and disclosure, using the Guiding Principles as the reference point.<sup>144</sup> These engagements cut across multiple sectors, including food and beverage, extractives, apparel, ICT, arms manufacturing, banks, private prisons, the automotive industry and tourism.

In 2019, the Investor Alliance for Human Rights led a broad coalition of investors in a public call for technology companies to implement the Guiding Principles, which led to a multi-year corporate engagement campaign.<sup>145</sup> In 2020, the Alliance also coordinated a group of 176 investors representing over US\$4.5 trillion AUM to call on the 95 lowest scoring companies on the 2019 CHRB's human rights due diligence indicators to publicly disclose how they identify, prevent, mitigate and account for how they address the most severe risks to people in connection with their businesses.<sup>146</sup> KraftHeinz, a low scoring company included in this group, later published a human rights policy and due diligence process in response to this effort.<sup>147</sup> The number of signatories has since grown to 208 investors representing over US\$5.8 trillion AUM.<sup>148</sup>

Investors are also coalescing around specific issues, such as forced labour and living wage. For example, 135 investors representing US\$5.8 trillion AUM joined forces to call on and directly engage the lowest scoring companies in the KnowTheChain apparel benchmark regarding their human rights due diligence practices and efforts to address forced labour.<sup>149</sup> The Platform Living Wage Financials (PLWF) is a coalition of investors engaging investee companies on the non-payment of living wages in global supply chains, as living wage was identified by members as a salient human rights issue connected to their investments that requires urgent attention by companies worldwide.<sup>150</sup>



Human rights-related shareholder proposals are also surging.<sup>151</sup> Indicating investor uptake of the Guiding Principles, resolutions filed in the 2020 proxy season called on companies to adopt human rights policies and board-level oversight mechanisms, conduct human rights impact assessments and disclose how a range of salient human rights issues are addressed. For example, Dutch asset management firm Robeco co-led the 2020 filing of a shareholder proposal at Google's parent company, Alphabet, asking for a Human Rights Risk Oversight Committee to be established. Around 40 percent of non-controlling shareholders voted in favour of the resolution and, in November 2020, Alphabet announced an update of its Audit Committee Charter to include the review of major risk exposures around human rights.<sup>152</sup>

In the 2021 proxy season, investors questioned brands on their role in contributing to racial disparities and pressed companies for paid sick leave as a standard benefit, as frontline workers including meat processing and retail workers continue to be at increased risk of exposure to COVID-19.<sup>153</sup> While it remains rare for the world's largest asset managers to vote in favour of ESG-related resolutions, BlackRock, for the first time, voted for a 2020 resolution calling on a food processing company to disclose its human rights due diligence.<sup>154</sup> In the 2021 proxy season, the asset manager reaffirmed its position by voting for the resolution again,<sup>155</sup> a move that was followed by Vanguard, the world's second largest asset manager.<sup>156</sup>

While not always aligned with the standards laid out in the Guiding Principles, investors and proxy advisory firms providing advice and recommendations to institutional investors have also started incorporating explicit human rights considerations into their proxy voting guidelines, thereby instructing shareholder representatives on how to vote on human rights-related resolutions.<sup>157</sup> For example, Aviva Asset Management has updated its voting policies to automatically vote against the board of companies that score poorly on the CHR. <sup>158</sup>

The positive developments notwithstanding, a 2020 study found that 61 per cent of asset managers surveyed had a weak or non-existent approach to engagement on human rights. Only a limited number of asset managers disclosed adequate approaches to engagement with companies on salient human rights impacts. It also found that managers primarily engaged companies on human rights once abuses had occurred, in many instances as a way to minimise financial risk to the portfolio, as opposed to proactively engaging companies on how they identify, prevent, mitigate and account for how they address human rights risks and impacts.<sup>159</sup>

Where investors engage on human rights, they often engage on individual human rights issues rather than promoting a holistic, governance-based approach to human rights risks management. Conversely, where investors prioritise good governance in stewardship activities, they do not often identify human rights responsibilities as essential board criteria or relevant to board oversight roles. Also, the depth of investor engagement with companies is often superficial – companies may satisfy investor requests by pointing to a policy that has not been implemented, and investors may also fail to dig deeper and track process due to limited time, data and capacity, among other factors.

Investor underperformance with regard to using leverage extends to proxy voting. A 2021 study found that asset managers primarily vote against social and environmental proposals, including human rights proposals. It also found that PRI signatories are not more likely to vote in favour of environmental and social proposals despite the fact that signatories promise to incorporate ESG issues

into investment analysis and decision-making processes.<sup>160</sup> One reason for this gap is likely the lack of widespread and consistent practice by asset owners in asking for asset managers to embed human rights due diligence across their investment activities.<sup>161</sup>

Private equity investors in particular are lagging with regard to using their leverage to respect human rights.<sup>162</sup> While general partners (GPs) in private equity tend to have high degrees of leverage and control over investee companies, as well as deep familiarity with the concept of due diligence, few appear to consider or act on human rights risks in their investment decisions.<sup>163</sup> In turn, although limited partners (LPs) in private equity – which includes most public pension funds and other institutional investors – have significantly less leverage than GPs to influence investee companies, very few LPs exercise the leverage they do have to further respect for human rights.<sup>164</sup>

### **Leading investors increase leverage by promoting enabling environments**

Where investors lack the necessary leverage to prevent or mitigate adverse impacts in investment portfolios through direct engagement with companies, the Guiding Principles expect investors to seek ways to increase their leverage. A key method used by investors in doing so over the past decade has been to collaborate with other investors. A less common yet noteworthy way has been to ensure that investment value chains respect human rights by engaging policymakers to support more robust requirements for their own business practices.

In 2019, investors representing nearly US\$2 trillion AUM called on EU Parliament and the United States Congress to require investors to carry out human rights due diligence and disclose their steps to address the adverse impact of their investment decisions on people and planet.<sup>165</sup> Investors also expressed their support for Australia's Modern Slavery Act, which requires companies and investors alike to disclose modern slavery risks in their value chains, explain any actions taken to address those risks and assess the effectiveness of those actions.<sup>166</sup> In December 2018, more than

70 large Dutch pension funds with nearly €1.2 trillion AUM also signed a covenant with the Dutch government, civil society organisations and trade unions committing to worldwide cooperation aimed at promoting sustainable investment based on respect for human and labour rights.<sup>167</sup>

Investor engagement with policymakers has also centred on ensuring that laws governing responsible business conduct by investee companies are in place and adequately enforced. For example, in 2020, investors representing US\$5 trillion AUM publicly called on governments to develop and enforce mandatory corporate human rights due diligence requirements as an essential step for investors to fulfil their own human rights responsibilities.<sup>168</sup> In late 2018, investors representing over US\$5 trillion AUM called on the U.S. Securities and Exchange Commission (SEC) to mandate corporate disclosure of ESG data, including human rights, which is a critical human rights due diligence step.<sup>169</sup> In 2020, the SEC took steps in this direction by mandating human capital disclosure by all companies selling securities in the United States.<sup>170</sup> And, on the sixth anniversary of the Rana Plaza Building collapse, a group of 190 investors led by the Interfaith Center on Corporate Responsibility (ICCR) and representing over US\$3 trillion AUM released a statement calling on the government of Bangladesh and the Bangladesh Garment Manufacturers and Exporters Association to negotiate an agreement allowing the Accord for Fire and Building Safety in Bangladesh to continue its work to protect the safety of garment workers and provide remedy for the impacts of the collapse.<sup>171</sup>

There are particular challenges in this area for sovereign bondholders, as investor engagement in a sovereign debt context can be misinterpreted as lobbying, advocacy or an attempt to interfere in governments' policy choices. As highlighted by the PRI, however, these investors can use the meetings they already have with sovereign officials to point out data needed to make more informed and responsible investment decisions, convey expectations and promote transparency and disclosure.<sup>172</sup> For example, Nordea Asset

Management's public decision to suspend the purchasing of Brazilian government bonds in response to the major Amazon forest fire outbreak in 2019 was followed by a meeting between the institution's leadership and Brazilian officials to discuss the extensive deforestation situation in Brazil, the firm's concern regarding the forest fires, the environmental consequences and the possible financial impact on the Brazilian economy.<sup>173</sup>

### Divestment practices are mixed

Investor efforts to mitigate human rights abuses by helping to shift corporate conduct should not be an indefinite process. As previously highlighted, where an investor lacks sufficient leverage to affect change in the behaviour of an investee company and is unable to increase its leverage, it may consider responsible divestment.<sup>174</sup> This includes going beyond adopting exclusionary screens focused on companies in certain industries or operating contexts to an approach that includes divestment decisions based on the assessment of corporate human rights performance, including progress over time, regardless of sector or operating context.

In practice, a number of investors who engage companies on human rights harms appear to be reluctant to set clear timelines for progress, which has resulted in well-documented examples of investee companies contributing to severe impacts over a decade without facing consequences on the part of investors.<sup>175</sup> In some cases, investors who choose to remain invested do not provide a public explanation of their decisions or provide evidence of continued due diligence. In other instances,

**In practice, a number of investors who engage companies on human rights harms appear to be reluctant to set clear timelines for progress.**

investors may silently divest from an individual company, missing the opportunity to be public and thereby exert greater pressure on the company and create leverage for affected rights-holders or others who have not divested.

These practices stand in contrast to notable examples of responsible divestment. For example, Storebrand Asset Management divested US\$34.8 million worth of shares in three companies with ownership in the Dakota Access Pipeline. Calling for respect for the right to free, prior and informed consent of impacted Indigenous groups, the asset manager sought to directly engage the relevant companies for months. It also joined a group of investors collectively aiming to influence the companies and organised a letter signed by 100 investors to the pipeline's creditors. When these efforts failed to change corporate conduct, Storebrand sold its shares and spoke publicly about its decision.<sup>176</sup> In Mexico, the Danish pension fund ATP decided to divest from the mining company Grupo Mexico in December 2019 after eight months of failed attempts to engage with the company over a new tailings dam and the associated risks to people and the environment in the state of Sonora. In particular, ATP expressed concern that an investment in Grupo Mexico would not allow the fund to live up to its commitment to the OECD Guidelines for Multinational Enterprises.<sup>177</sup>

### **Investor transparency and disclosure remain limited**

Like investee companies, investors should formally disclose how they take action to prevent, mitigate and address severe human rights risks and impacts. Yet a 2020 study found that insufficient reporting from asset managers leaves clients unclear about the degree to which human rights policy commitments are translating into action. Only 17 percent of assessed asset managers publicly disclosed a comprehensive record of ESG-related engagements, and only 12 percent of managers publicly disclosed the names of excluded companies.<sup>178</sup> A 2021 study assessed the disclosure of 79 asset managers required to report under the UK Modern Slavery Act and found that 53 percent failed to meet the minimum requirements

of the law.<sup>179</sup> The problem of investor transparency is especially pronounced in private equity.<sup>180</sup>

This disclosure landscape poses challenges for assessing what institutional investors are doing to translate their commitments into action (e.g., engagement activities and voting practices), and the effectiveness and impacts of these practices. It also undermines the ability of rights-holders and other stakeholders to identify and engage investors in companies responsible for human rights abuses. However, examples of investor disclosure aligned with the spirit of the Guiding Principles are emerging. In 2019, the Swedish pension fund AP2 became the first asset owner to publish a human rights report in line with the UN Guiding Principles Reporting Framework,<sup>181</sup> and ABN AMRO's Human Rights Report, also based on the UN Guiding Principles Reporting Framework, details how the Dutch bank, within its function as an investment manager, seeks to encourage clients to invest in companies that respect human rights.<sup>182</sup> The Council on Ethics for the Norwegian Government Pension Fund Global also reports annually on its actions related to its human rights criterion, including information on its in-depth human rights investigations into certain sectors (for example, 'beaching' in India and Bangladesh), substantive company dialogues, engagements with civil society organisations and recommendations for exclusion or observation of specific companies.<sup>183</sup>

### **Access to remedy for victims requires urgent attention**

The institutional investor community has yet to grapple with its responsibility to provide or enable remedy for victims as it relates to its investment activities. Although the business and human rights community has explored the role of financial institutions such as banks in the context of project lending to provide or enable remedy, sufficiently less attention has focused on the role of asset owners and managers. In practice, very few firms have in place mechanisms that would enable victims or their representatives to raise grievances about portfolio companies. Moreover, even responsible investors rarely engage portfolio companies on the effectiveness of company grievance mechanisms



and to promote trade union rights and whistleblower protections. As a result, portfolio companies are rarely pressured by investors to provide remedy to people who have been harmed.



While still rare, some investors are making increased efforts to enable access to effective remedy for victims of business-related human rights abuse. As highlighted above, Sycomore Asset Management adopted a stand-alone human rights policy that includes a commitment to develop a grievance mechanism for stakeholders to submit feedback regarding the firm's investments.<sup>184</sup> The Dutch Pension Funds Agreement on Responsible Investment requires investor parties to 'use and, where necessary and possible, increase leverage by imposing time-limited demands in which it encourages listed investee companies that cause or contribute to an adverse impact to... provide access to remediation.'<sup>185</sup> The Finnish Fund for Industrial Cooperation (Finnfund), in its human rights statement, commits to promoting effective access to remedy for those who have been harmed and using its leverage to have adverse human rights impacts addressed.<sup>186</sup> Companies financed by Finfund are also required, as appropriate, to have an effective operational level grievance mechanism to facilitate non-judicial access to remedy.<sup>187</sup> FinDev Canada, the investment function of Export Development Canada, also commits the institution to playing a role in enabling remedy and using its leverage to encourage responsible parties to provide appropriate forms of remedy.<sup>188</sup> Although these limited examples have largely been in the form of commitments rather than direct

action, public acknowledgement of the important role that investors play in the remedy ecosystem is a significant development.

### Human rights are not yet fully integrated across ESG siloes

Persistent siloes between investor action on E, S and G issues constitute a barrier for progress in light of the human rights implications of corporate governance and environmental impacts. For example, while investors increasingly ask companies to act on climate change risks, only a handful of investors call on companies to conduct and disclose 'climate due diligence,' which integrates human rights due diligence and climate action.<sup>189</sup> Also, while some investors engage companies to drive responsible lobbying practices and strengthen corporate governance,<sup>190</sup> these efforts do not call on companies to assess and address how such lobbying practices undermine human rights.

These siloes are a barrier for holistically tackling risks to people given the cross-cutting nature of human rights. In 2019, the UN High Commissioner for Human Rights warned that the worsening climate crisis is the greatest threat to human rights around the world,<sup>191</sup> impacting the rights to life, health, water, food and an adequate standard of living.<sup>192</sup> It is also imperative that human rights risks are addressed by renewable energy companies if the sector is to continue to grow at the pace needed to tackle the climate crisis. In 2018, former UN Secretary General Ban Ki-moon also recognised the failure of good governance and responsible lobbying practices as threats to human rights.<sup>193</sup>

This barrier is compounded by insufficient alignment between methodologies used by many data providers, rankings and benchmarks and the Guiding Principles. For instance, benchmarks that evaluate human rights have yet to include key indicators that assess human rights due diligence as it relates to political engagement activities,<sup>194</sup> whereas benchmarks evaluating political donations or lobbying do not use a human rights lens to evaluate company policies and practices.<sup>195</sup> In addition, while the Climate Action 100+ initiative has issued a Net Zero Company Benchmark evaluating companies on greenhouse gas emissions, it has

yet to align its just transition indicator with human rights due diligence.<sup>196</sup>

On the other hand, emerging examples of investor action across often-siloed ESG areas show that bridging these gaps is possible. For example, Investor Advocates for Social Justice, which represents a coalition of faith-based investors, has called on its members' investee companies to ensure that human rights due diligence is part of the transition to a low-carbon economy.<sup>197</sup>

### Heightened due diligence for conflict-affected contexts is lacking

Investor practice overall falls short in conducting heightened due diligence and adjusting financial capital flows away from business activities connected with highly severe human rights impacts, including in conflict-affected contexts. This lack of standardised and effective human rights due diligence is the result of several factors: the 'siloing' of conflict as one human rights issue among many, as opposed to a contextual lens through which a broad range of risks may be analysed; a limited understanding among investors of the regulatory (e.g., targeted sanctions) risks associated with conflict; and the difficulties in accessing information on the human rights harms of business activities and value chain partners in these complex and opaque environments.

These shortfalls have resulted in inconsistent investor responses to the presence of human rights harms in investment portfolios. For example, the high occurrence of holdings in investee companies with activities in settlements on occupied Palestinian territory testifies to insufficient awareness of the responsibility incumbent on enterprises 'directly linked' to these activities. Even companies engaged in exploitation of natural resources on territories legally recognised internationally as occupied regularly appear in the investment portfolios of banks, pension funds and sovereign wealth funds without raising any red flags.<sup>198</sup> In the Democratic Republic of the Congo, a number of pension funds, foundation trusts and university endowments have been linked, through limited partnerships and layers of ownership, to documented human rights abuses against local communities.<sup>199</sup> Dutch pension

funds, through their asset managers, have also been recently documented as collectively holding US\$2.3 billion in 20 companies with direct and long-standing ties to the Myanmar military, responsible for genocidal acts against the Rohingya<sup>200</sup> and for carrying out a coup against the democratically-elected government in February 2021.<sup>201</sup>

These and other cases notwithstanding, examples of investor due diligence in high-risk or conflict-affected regions illustrate what is possible. For example, in April 2021, investors representing \$4.4 trillion in AUM used their leverage to engage 47 companies in eight sectors with potential links to forced labour or surveillance in Xinjiang, China.<sup>202</sup> They called for disclosure of company value chains, in and outside of China, and the steps taken by companies to disengage from business relationships connected with human rights harms in the region.<sup>203</sup> In 2021, APG engaged the South Korean steel producer Posco C&C over human rights concerns connected to its relationship with the military junta in Myanmar. The company responded by announcing it would end its relationship with the military-owned company, Myanmar Economic Holdings Limited.<sup>204</sup> Investors are also collaborating with civil society to build their capacity and develop guidance. For example, Achmea Investment Management worked with the civil society organisation PAX in developing public investor guidance on navigating conflict-related human rights risks.<sup>205</sup> Heartland Initiative works directly with a number of institutional investors to implement rights-respecting investment practices in conflict-affected and high-risk areas.<sup>206</sup>

### Investor-stakeholder engagement is informing investor due diligence in some cases

While some investors will respond to and engage with victims of adverse corporate impacts, civil society organisations, trade unions and human rights defenders<sup>207</sup> that provide information on the real-world impacts of companies, stakeholder engagement among investors is still rare. Investors rarely have the systems and processes to receive, respond to or engage with the grievances of affected rights-holders or those representing them. Where investors respond, they may deem information as

insufficient to warrant taking action. In the context of reprisals against human rights defenders, this is particularly problematic. Investors may be reticent to engage given the challenges in linking causation or contribution to a portfolio company, even where defenders are raising concerns related to a company's specific project.

In cases where investors respond to grievances and engage with civil society to raise concerns with investee companies, the majority do not publicly disclose information about these engagements and the associated outcomes. Some investors and civil society organisations have noted that there is also a power imbalance in the context of their engagements—investors may control the narrative with companies, while companies put constraints on who can join engagements. As a result, rights-holders and their representatives may be sidelined from key discussions and decisions that directly affect them.

Moreover, investor uptake of the stakeholder engagement aspect of human rights due diligence can be challenging based on the fact that financial actors often lack direct relationships with impacted rights-holders. However, some investors have demonstrated creative and meaningful ways of taking this step over the past decade. For example, after the catastrophic tailings dam failure at Vale's Brumadinho mine in Brazil, the Church of England Pensions Board and the Swedish Council of Ethics of the AP Funds led the formation of the 'Investor Mining & Tailings Safety Initiative,' with the goal of facilitating investors in extractive industries to engage with impacted communities, experts, government representatives and company representatives.<sup>208</sup> A group of investors also engaged in a site visit to the Fair Food Program, led by the Coalition of Immokalee Workers, in January 2020, in order to build the capacity of investors to promote the worker-driven social responsibility model,<sup>209</sup> and investors subsequently used these learnings to inform a successful shareholder proposal to encourage adoption of this effective model.<sup>210</sup> Another example is the Committee on Workers Capital, established in 1999, bringing together labour unions and asset owner board members from around the world to promote information sharing and joint action in building long-term value and integrating ESG issues into the

stewardship of pension funds.<sup>211</sup>

Civil society advocacy campaigns in Mexico have also organised and supported communities affected by mining and wind turbine projects by directly engaging with company shareholders to raise concerns about the real and potential impacts of these projects on their communities.<sup>212</sup> Labour groups such as UNI Global Union have informed investors of labour rights practices among investee companies,<sup>213</sup> and civil society has played a key role in amplifying the voices of Indigenous Peoples in North America, Latin America and Southeast Asia, as well as affected communities in Africa.<sup>214</sup> Such efforts have led to a range of investor engagements with investee companies,<sup>215</sup> informed shareholder resolutions and decisions to divest<sup>216</sup> and, in some instances, led to the creation of targeted investor initiatives, such as the Investors & Indigenous Peoples Working Group.<sup>217</sup>

In a uniquely innovative example of partnership between an investment institution and a civil society organisation, La Banque Postale Asset Management (LBPAM) manages Libertés & Solidarité, a socially responsible investment fund created by FIDH, the second oldest international human rights organisation.<sup>218</sup> The fund aims to encourage governments to actively promote human rights and businesses to adopt socially responsible behaviours through the inclusion of human rights criteria in its selection of stocks and bonds.

### **Passive investment poses unique problems that require attention**

There has been a significant shift in recent years from active to passive investment across public equity and fixed income investments, which constitute the largest share of capital markets globally.<sup>219</sup> In 2019, passive equity investments surpassed active investments in the United States and continue to rapidly gain market share. The trend is also global, as European equity markets are now approximately 33 percent passive and Asian equity markets about 50 percent passive. In China, passive equities are growing faster than any sector, currently at around ten percent of the market.<sup>220</sup>

Broadly speaking, passive investing has had the effect of rearranging power and leverage in the



financial system, away from asset owners to asset managers. Fund managers carry out investments on a day-to-day basis on behalf of asset owners (for example, workers' pension funds) who can be highly disaggregated, making leverage highly diffuse. The average asset owner is so small relative to the total AUM of the largest asset managers that they have little control or leverage over allocation strategies. Asset owners seeking change in their investment strategies, particularly on ESG issues including human rights, are therefore increasingly frustrated by a lack of action from asset managers. Reflecting this, pension plan managers representing US\$2.43 trillion AUM have stated that index managers were not meeting their stewardship goals at all, while 23 percent said they were only meeting them 'to a limited extent.'<sup>221</sup>

Data shows that large and passive asset managers vote significantly less in favour of social and environmental shareholder proposals, including those related to human rights. Because passive funds are homogeneous, asset managers primarily compete on costs, resulting in downward pressure on fund expense ratios. One resulting area of cost saving for passive investors has been standardising voting and engagement with the goal of becoming a low-cost leader on index investments.<sup>222</sup>

Given marketplace trends that point to increased passive investment, increased attention to how passive investors—owners and managers—uphold their human rights responsibilities is necessary. The investor responsibility to respect human rights is applicable to all investment activities, products

and services offered by institutional investors, including passive investing.

### **Other investment ecosystem actors are not yet stepping up to the plate**

While the key actors in implementing investor respect for human rights are investors themselves and governments as duty-bearers in protecting human rights, other business actors that work within the investment ecosystem have their own responsibilities to respect human rights under the Guiding Principles.

To date, however, key players such as data service providers, proxy advisors, stock exchanges, credit rating agencies, placement firms, investment consultants and other actors are not sufficiently integrating human rights considerations in the products and services that they provide. As a result, the data and advisory services used by investors often contradict what investors are expected to know or do to uphold their responsibility to respect human rights. Significantly greater efforts are needed to ensure that ecosystem actors refer to international human rights standards and frameworks in their activities, products and services. This includes ensuring they use a lens of risk to people when evaluating and rating investees on ESG risks and performance, moving beyond the narrow focus of human rights as a relatively small set of issues, and aligning reporting standards and guidance with the Guiding Principles.





# Conclusion and key recommendations for increasing investor action in the next decade

The Guiding Principles provide a framework for building and driving financial markets based on the protection of and respect for people's fundamental welfare and dignity. Without urgent action by institutional investors and those that work with and influence them to embed respect for human rights in corporate ownership, finance and governance, corporate respect for human rights risks will be stymied in the decade ahead. A widespread and serious embrace of long-term thinking and decision-making within investment institutions and the full spectrum of actors they work with is an essential and core component of any meaningful shift to responsible investment. Doing so will require building on promising practices and addressing the key gaps and barriers outlined in this report. The decade ahead presents real and practical opportunities for a new era of rights-based investment.

The following recommendations focus on how (1) States, (2) institutional investors and (3) other actors in the investment ecosystem can advance the investor responsibility to respect human rights over the course of the next decade, and beyond. Each set of recommendations starts with priorities for the near-term and progressively builds to more advanced practice. Depending on location, size and positioning within the investment ecosystem, different actors will have different entry points into the recommendations below and different paths toward continuous improvement.

The Working Group will promote these recommendations across stakeholder groups, throughout its own activities and in the UNGPs 10+ Project Roadmap to be released in late 2021.



## Recommendations for States

States have a key role to play in advancing investor respect for human rights, including a building block towards successfully transitioning to a form of stakeholder capitalism that is based on respect for human rights. The Guiding Principles call on all States to take all appropriate steps to prevent, investigate, punish and redress abuses connected to investment value chains through effective policies, legislation, regulations and adjudication. Such efforts should ensure and promote responsible investment practices among all institutional investors, including public equity investors, private equity firms, venture capitalists and hedge funds.

### **A. Provide investors with guidance on how to integrate human rights into investment practices**

- Support the creation of guidance for institutional investors, including public pension funds, sovereign wealth funds, development finance institutions, as well as small and medium-sized investment firms, on respecting human rights throughout their investment activities, including on how this relates to fiduciary duties and to broader sustainability and ESG investing.
- Support, facilitate and participate in multi-stakeholder platforms to promote dialogue on institutional investment and human rights, analyse ways to address human rights risks in investment activities and strengthen monitoring and accountability.

### **B. Ensure that State institutions dealing with investment uphold the States human rights obligations and ensure policy coherence across institutions**

- Ensure that State institutions dealing with institutional investment have the mandate, skills and resources to promote investor respect for human rights.
- Develop and implement policies for cross-government alignment of Guiding Principles implementation activities with legislative, regulatory, policy and adjudicative efforts related to institutional investment.
- Commit to specific, future-oriented actions to promote respect for human rights among institutional investors and their ecosystem, for example, in national action plans on business and human rights.
- Promote policy coherence regarding the human rights responsibilities of investors in the context of State institutions tasked with promoting sustainable economic development. Particular attention should be placed on the role of investors in encouraging companies to carry out human rights due diligence as the first step towards the realisation of the Sustainable Development Goals of the 2030 Sustainable Development Agenda.
- Ensure State efforts to advance responsible investor conduct recognise the alignment between the expectations laid out in the Guiding Principles and in key global frameworks, such as the OECD Guidelines for multinational enterprises, the guidance for institutional investors on due diligence under the OECD Guidelines and the G20/OECD Principles of Corporate Governance.
- Refer to the Guiding Principles to promote shared understanding of the human rights responsibilities of investors when negotiating international investment agreements, as well as developing international and regional standards for responsible investment practices.

**C. Take additional steps to protect against human rights abuses of investment activities owned or controlled by the State**

- Integrate respect for human rights into the mandate, operations and investment activities of institutions involved in the issuance and management of State pension funds, sovereign wealth funds and development finance.
- Assess whether policies and legislation relating to public pension funds, sovereign wealth funds and development finance institutions are aligned with the State's human rights obligations and address gaps.

**D. Strengthen relevant regulatory frameworks**

- Strengthen implementation of relevant legislation and codes, including ESG requirements for asset owners and asset managers, and clarify how these relate to human rights.
- Mandate corporate (investee) human rights due diligence in line with the Guiding Principles to support institutional investors' efforts to assess and address human rights risks in investment portfolios.
- To the extent that the State requires companies act with human rights due diligence, these requirements are inclusive of institutional investors and financial institutions in general.
- Require institutional investors to conduct and disclose human rights due diligence efforts in line with the Guiding Principles, for example, by introducing or strengthening legislation and by clarifying that fiduciary duties require investors to align their investment practices with the responsibility to respect human rights at each phase of the investment cycle.
- Address investor short-termism and encourage longer-term investments, for example, by imposing greater taxes on short-term capital gains relative to long-term capital gains, reforming disclosure requirements to align with longer periods of time and placing greater scrutiny on derivative trading or other practices/products that contribute to short-termism.

### *Recommendations for Institutional Investors*

To fulfil their responsibility to respect human rights, institutional investors should take all necessary steps to avoid infringing on human rights throughout their investment activities and address adverse human rights impacts with which they are involved.

The following recommendations provide an overview of key steps investors are expected to take to uphold their human rights responsibilities. These steps do not suggest a linear process, recognising that different investors will be stronger in certain areas and weaker in others. Investor due diligence is a process of continuous improvement and should begin with identifying gaps in existing practice and prioritising action based on the abovementioned human rights criteria. In this journey, a cross-cutting priority for investors is the need to significantly strengthen internal capacities on business and human rights as a crucial first step for understanding and meaningfully engaging with the investor responsibility to respect human rights.

#### ***A. Articulate commitment to respecting human rights and embed this commitment in corporate governance and across all investment activities***

- Adopt a policy commitment to respect internationally recognised human rights in line with the Guiding Principles. The commitment should be adopted by the board of directors and should apply to the institution's own operations, all investment activities and the full value chain. It should also set out expectations for employees and the full range of business relationships, including investees, investment analysts, clients, asset managers, financial advisors and trade associations.
- Embed the commitments throughout the investment firm, for example, by hiring in-house human rights expertise, training staff tasked with investment decision-making and stewardship on human rights, ensuring performance targets do not hinder human rights due diligence and integrating the human rights commitments into other investment policies, codes of conduct and limited partnership agreements.
- Embed the policy coherently across all investment activities, including those that seek to have positive impacts such as impact investing activities, investing aimed at contributing to the Sustainable Development Goals and efforts to meet the standards laid out in the Paris Climate Agreement.

#### ***B. Screen investment portfolios for real and potential adverse human rights impacts***

- Assess the actual and potential human rights impacts of investees prior to investing and on an ongoing basis once invested. This involves assessing the investees' human rights policies, processes; management of their respective salient human rights issues; business model red flags that increase the likelihood of human rights harms; and the real-world impacts of the company on people, including the real-world outcomes of their due diligence efforts.
- Where investment portfolios are especially large, use a 'risk-based approach' to identify particularly high risk sections of portfolio where the risk of adverse impacts is most significant. Based on this assessment, prioritise investees for further assessment. High-risk factors to consider include geography, sectors, business models, products and services.

- As part of efforts to meaningfully assess the human rights performance of investees and address challenges in the data landscape, consult with relevant stakeholders, such as civil society organisations and trade unions.
- Engage ESG reporting frameworks, benchmarks and data providers to ensure that the research methodologies, corporate performance data and advisory services used to assess investees are aligned with the Guiding Principles and reflect real-world outcomes for people. Where necessary, commit to supporting the development of new frameworks or better approaches to evaluating human rights performance.

### ***C. Where risks or adverse impacts are identified, take appropriate action***

- Engage investees in constructive dialogue to promote: (1) the adoption of human rights policies, governance, due diligence and effective grievance mechanisms and (2) the provision of remedy for victims of human rights abuse.
- Where prioritising action to address actual and potential adverse human rights impacts may be necessary, investors prioritise existing or potential investees that are actually, or likely to be, associated with more severe risks (as a function of its scale, scope and irremediable character).
- Engage portfolio companies to address root causes of short-termism, for example, by:
  - a. Calling for integration of human rights into governance expectations and board committee responsibilities;
  - b. Tying executive pay to corporate human rights performance;
  - c. Asking investee companies for long-term plans and cumulative earnings reporting in which each quarter builds on the next (three months, six months, nine months and then the full year), which leaves in place the transparency of regular reporting while avoiding the quarter-to-quarter comparisons that drive short-term behaviour;
  - d. Elevating stakeholder voice and perspectives in corporate governance and ownership structures, such as by reserving board seats for employees, promoting opportunities for employee ownership and supporting the adoption constituency statutes and reforms of corporate ownership law; and
  - e. Engaging peers whose investment practices pressure boards to prioritise short-term returns over human rights and long-term sustainability.
- In the case of private equity and venture capital investors, ensure that any business model features that pose human rights risks are identified and adapted to prevent and mitigate any future human rights harms.

### ***D. Where initial use of leverage is insufficient to create change, seek to increase leverage***

- In the context of public equities, file and support shareholder proposals that reflect the expectations of the Guiding Principles.
- Develop proxy voting guidelines that reflect a commitment to human rights, engage in proxy voting in line with that commitment and publish a proxy voting report.

- Participate in peer-to-peer and multi-stakeholder platforms that promote business respect for human rights and set out an expectation that investee companies also engage with these platforms.
- Responsibly engage policymakers and standard-setting bodies – including governments, international organisations, courts and industry associations – to tackle systemic human rights risks and create enabling environments for responsible business conduct that is grounded in respect and accountability for human rights.

### ***E. Track the effectiveness of your efforts to exercise leverage***

- Track effectiveness of due diligence efforts, for example, by monitoring voting decisions of the institutions that vote the firm's proxies and holding them accountable, by requiring all portfolio companies to disclose corporate human rights performance data that goes beyond inputs, activities and outputs to include information on outcomes for people and through ongoing engagement with relevant stakeholders.

### ***F. Disclose how you manage human rights risks***

- Formally and publicly disclose how the institution is addressing salient human rights risks and impacts connected with investment activities.

### ***G. Responsibly divest, where appropriate***

- Where an investor lacks the leverage to prevent or mitigate adverse impacts and is unable to increase its leverage, it should consider ending the relevant business relationship. For active strategies, this will involve divestment. For passive strategies, where possible and in compliance with regulatory obligations, investment strategies may be redesigned, for example, by exiting a passive index and investing in an adjusted or tailored index which excludes severe risks identified by the investor, including based on operating contexts or sector-specific risks.
- When the investor does divest, publicly communicate why the firm has redirected its investments, in order to help maximise the institution's leverage and create leverage for others.

### ***H. Take steps to promote and enable access to remedy for victims***

- Where the investor is linked to the human rights harm through its investees, use and build the institution's leverage to promote and enable the provision of remedy for victims of business-related human rights abuse, including by recalling the expectation that the investee company have in place an individual operational-level grievance mechanism or by participating in collective platforms in line with the Guiding Principles' effectiveness criteria.
- Have in place effective operational-level grievance mechanisms to support the provision of remedy when the institution has caused or contributed to adverse human rights impacts, such as in the context of its own employees or other stakeholders affected by the investor's operations or where the firm's investment-level due diligence was sub-standard and resulted in contribution.



## Recommendations for other actors in the investment ecosystem

A key element for achieving progress in the next decade will be to advance awareness and understanding of human rights standards in general and the Guiding Principles framework in particular, throughout the investment community. This includes within the ESG and impact investing fields, where discussions on what constitutes responsible investment primarily reside. Embedding business and human rights across these spaces—including through capacity building, monitoring and accountability—will help to significantly scale the uptake of the Guiding Principles among investors and broader economic actors as a result.

### A. Investor associations and networks

- Build internal capacity around rights-respecting investment and offer specific guidance for members on the investor responsibility to respect human rights, including in relation to: (1) how to reconcile an investor's fiduciary duties and its responsibility to respect human rights; (2) how to identify and prioritise companies for engagement within investment portfolios; and (3) practical case studies of investor due diligence across asset classes.
- Use convening power to share learnings, challenges and good practices among institutional investors, as well as to use collective leverage to influence standard-setting bodies in the direction of alignment with the Guiding Principles.
- Call for alignment of ESG benchmarks, data providers and reporting frameworks with the Guiding Principles.
- Set requirements for investor members to implement the Guiding Principles and hold investor members accountable for underperformance on embedding respect for human rights in investment decisions and stewardship activities, including proxy voting.

### B. Regional and international organisations, including the UN

- UN agencies, treaty bodies and special procedures use and promote the recommendations in this report, where relevant. This should include developing tailored recommendations for investors that acknowledge the differing size and capacity of, as well as the leverage tools available to, investment institutions.
- Promote the investor responsibility to respect human rights in efforts to mobilise private investment for sustainable economic development, including the realisation of the 2030 Sustainable Development Agenda.

### C. Civil society organisations, academia and research institutions

- Increase internal capacity on the intersection of investment and human rights, as well as the range of investment tools and actors, such as data service providers and credit rating agencies, in order to enhance the efficacy of stakeholder engagement with the investment industry.
- Gather and communicate data relevant to institutional investors and their human rights



commitments and performance, including outcomes for people, in order to facilitate the identification of gaps and good practices and inform investor due diligence.

- Develop practical guidance and tools for investors on rights-respecting investment practices across the full investment lifecycle, as well as across asset classes and investment strategies.
- Collaborate with and support responsible investors to promote respect for human rights in investment portfolios, for example, by directly advising investors on rights-respecting investment, collaborating with investors on developing shareholder proposals and participating in corporate accountability campaigns alongside investors.
- Dedicate increased attention to the investor responsibly to respect human rights, including in terms of accountability under national, regional and international laws.





# Glossary

**Active ownership:** Active ownership policies and practices entail the use of the rights and position of ownership to influence the activities or behaviour of portfolio companies. Active ownership can be applied differently in each asset class. For listed equities, it includes engagement and voting activities.

**Asset:** An asset is a resource with economic value that may be owned or controlled by an individual or a company with the expectation that it will provide a future benefit.

**Asset class:** A grouping of investments with similar characteristics. Types of asset classes include equities (stocks), fixed income (bonds, including credit ratings and private debt), cash and cash equivalents, private equity, real estate, infrastructure, commodities, futures and other financial derivatives.

**Asset owners:** Owners have the legal ownership of assets. They include sovereign wealth funds, pension funds, insurance funds, churches, charities, foundations, family offices, multi-family offices and providers.

**Asset managers:** Manage investments on behalf of others. They determine what investments to make or avoid in order to grow a client's portfolio over time. Managers include investment funds, insurance companies and pension funds.

**ESG:** Stands for environmental, social and governance. A generic term used by investors to evaluate corporate behaviour and to determine the future financial performance of companies. ESG factors are a subset of non-financial performance indicators that drive responsible investment decision-making and active ownership.

**Exchange-traded fund (ETF):** ETFs are a basket of securities traded on stock exchanges. They are similar in many ways to mutual funds, except that ETFs are bought and sold throughout the day on stock exchanges while mutual funds are bought and sold based on their price at day's end. ETFs can contain many types of investments, including stocks, commodities, bonds or a mixture of investment types.

**Fiduciary duty:** A fiduciary is a person or organisation that acts on behalf of another person or persons to manage assets. A fiduciary owes to that other entity the duties of 'good faith and trust.' In general, asset managers and asset owners are considered to be fiduciaries.

**Fund of funds (FOFs):** A pooled investment fund that invests in other types of funds. In other words, its portfolio contains different underlying portfolios of other funds. FOFs typically invest in other hedge funds or mutual funds.

**Hedge fund:** A form of alternative investments using pooled funds. They are actively managed and have the ability to make more extensive use of leverage and more complex investment techniques as compared to regulated investment funds, such as mutual funds and ETFs.

**Investment strategy:** A plan designed to help individual investors achieve their financial and investment goals. Plans range from conservative to highly aggressive and include value and growth investing.

**Materiality:** Material events or information are considered events or facts that an informed investor would consider important in making an investment decision. Material issues can have a major impact on the financial, economic, reputational and legal aspects of a company and financial returns for investors.

**Minority shareholder:** A shareholder who owns less than half the total shares of a company.

**Multi-asset strategy:** This strategy combines different types of assets to create a diversified investment portfolio. Fund managers make big-picture decisions and balance asset classes to achieve particular investment outcomes, such as growth, income or risk minimisation.

**Mutual fund:** A managed investment fund that pools money from many investors to purchase a wide range of securities.

**Passive investment:** Also known as index investing, whereby investors purchase a representative benchmark, such as the S&P 500 index and hold it over a long time horizon.

**Pension funds:** Pooled monetary contributions from pension plans set up by employers, unions or other organisations to provide for their employees' or members' retirement benefits. Pension funds are the largest investment blocks in most countries and dominate the stock markets where they invest.

**Private equity:** An alternative investment class consisting of equity securities of unlisted (private) companies. Private equity funds are generally organised as limited partnerships. Limited Partners (LP) typically own most of the shares in a fund and have limited liability, while General Partners (GP) own a small percent of shares and have full liability. GPs are responsible for executing and operating the investment.

**Public equity:** Shares of ownership issued by publicly listed companies and traded on stock exchanges. Investors may profit from equities through a rise in the share price or by receiving dividends. Unlike private companies, public companies have gone through rigorous approval processes in order to participate in the public market, making it easier for investors to buy and sell company shares at any time. Public companies are required to regularly

publish detailed financial results.

**Shareholder engagement:** Any interactions between the investor and current or potential investee companies on ESG issues, including human rights, with the goal of improving practices and/or improving disclosure. It involves a structured process that includes dialogue and continuously monitoring companies. Engagements may be conducted individually or jointly with other investors.

**Sovereign wealth fund:** A state-owned investment fund that invests in real and financial assets such as stocks, bonds, real estate, precious metals or in alternative investments such as private equity fund or hedge funds. The fund's money is often derived from a country's surplus reserves, such as natural resource revenues, trade surpluses and money from privatisations.

**Security:** A security is a tradable financial asset. There are primarily three types of securities: equity—which provides ownership rights to holders; debt—essentially loans repaid with periodic payments; and hybrids—which combine aspects of debt and equity.

**Voting:** The exercise of voting on management and/or shareholder resolutions to formally express approval or disapproval on relevant matters, including human rights-related concerns. This involves taking responsibility for the way votes are cast on topics raised by management, as well as submitting resolutions as a shareholder for other shareholders to vote on (in jurisdictions where this is possible). Voting can be done in person, during an Assembly General Meeting (AGM) or by proxy.

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**Without urgent action by institutional investors and those that work with and influence them to embed respect for human rights in corporate ownership, finance and governance, corporate respect for human rights risks will be stymied in the decade ahead.**