SUBMISSION TO THE UN Working Group on Business and Human Rights

October 13, 2023 – Inspiration on how to apply the UNGPs to Responsible Investments (ESG)

Table of Contents

1. Introduction ... ***2***
1.1 Is it necessary? – are investors also bound by the UNGPs ... 3
1.2 Limitation of the guide ... 5
1.3 Preliminary clarifications ... 6

2. Embedding Responsibility with Investors ... ***8***

2.1 Before Investing ... **9**
Step 1: Implementing in own operations ... 9
Step 2: Develop Requirements ... 10
Step 3: Screening procedure ... 13
Step 4: Decision to invest and evaluating opportunities for improvement ... 14

2.2 After Investing ... **15**
A: Ex Ante ... 15
B: Ex Post ... 17

3. Overview of Due Diligence Process ... ***21***

This draft guide to investors on how to implement the UNGPs in practice is built on GLOBAL CSR's contributions from 2020 to the Investor Alliance for Human Rights: "Investor Toolkit on Human Rights" (https://investorsforhumanrights.org/sites/default/files/attachments/2022-03/Full%20Report%20Investor%20Toolkit%20on%20Human%20Rights%20May%202020_updated.pdf).

The present draft was updated with subsequent experiences, insights, and practises by the authors:
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It is our hope that the contribution can assist the UN Working Group on Business and Human Rights in advancing the scaling up of 'respect for human rights' with business enterprises all over the world as envisioned through the tremendous efforts of late Prof. John G. Ruggie, when creating the foundation for such change with the UNGPs.

Copenhagen, 13. October 2023.

1. Introduction

This guidance provides investors with assistance to improve alignment of approaches to ESG/SRI practices with the globally agreed minimum standard for responsible business conduct: The UN Guiding Principles on Business and Human Rights (the UNGPs) that was unanimously endorsed by the UN Human Rights Council in 2011.

The Sustainable Development Goals or Creating Shared Value and the UNGPs

Companies often engage in philanthropic activities, in strategic CSR or Creating Shared Value for a variety of stakeholders. From 2015 to 2030 many such activities are directed towards the fulfilment of the Sustainable Development Goals (SDGs), thereby enhancing the opportunity of governments to meet the goals. All these activities are meaningful and will in many ways improve the world we live in.

However, they are all voluntary. Corporate accountability around the SDGs will not be agreed and established by UN before their expiry in 2030. Indeed, seeking to benefit from contributions to the SDGs while not aligning with the UNGPs will increase beneficiary companies' exposure to criticism. The UNGPs are very clear on the subject in the commentary to foundational principle 11:
"*Business enterprises may undertake other commitments or activities to support and promote human rights, which may contribute to the enjoyment of rights. But this does not offset a failure to respect human rights throughout their operations.'*"

The guidance provides simple, practical answers to the questions:

- *What impact does the UNGPs have on "Environmental, Social and Governance (ESG)" work or "Socially Responsible Investment (SRI)" approaches for investors? and,*
- *What are the practical steps for investors to ensure compliance with the UNGPs?*

The UNGPs are globally agreed upon through the UN as a pragmatic solution to the question that all businesses would like to answer affirmatively: Do you respect human rights?

Decades of uncertainty about how businesses should take responsibility for impacts on human beings in our societies ended in 2011. The bar has been set relatively high; however, neither investors, nor other businesses, any longer need to invent or develop their own standards to which they seek to hold each other accountable for responsible business conduct. Distinct from how 'respect for human rights' is defined for states, business 'respect for human rights' has been defined through key elements of a management system, that all businesses can, and should, expect to be implemented from each other. States have, under existing human rights hard law obligations, the duty to regulate businesses within their territory to 'respect human rights'.

UNGPs Foundational Principle 2.
"States should set out clearly the expectation that all business enterprises domiciled in their territory and/or jurisdiction respect human rights throughout their operations."

In recent years, several states around the world have embarked on regulation to meet the obligation. The EU has explicitly based the Taxonomy Regulation requirement to meet the 'minimum safeguards', the Corporate Sustainability Reporting Directive (CSRD), and the upcoming Corporate Sustainability Due Diligence Directive (CSDDD) on the UNGPs.

The global authoritative minimum standard for managing adverse impacts on social sustainability apply to all businesses, also investors. To comply with the UNGPs, investors must adopt a policy commitment, have in place human rights due diligence, and ensure access to remedy through effective grievance mechanisms.

Like any other businesses, all investors may cause, contribute, or be linked to potential or actual adverse impacts on human rights, which they need to manage in accordance with the UNGPs. In addition, investors, as any other business, should expect from their business relationships that they 'respect human rights', i.e., implement a management system that meets the bare minimum outlined by pillar II in the UNGPs.

The UNGPs form the global minimum standard for how investors should manage adverse human rights impacts. Other international standards and guidelines can help inform how best to address the adverse impacts identified, e.g., in specific sectors. However, committing to, following or using other voluntary guidelines or standards cannot substitute the implementation of the UNGPs.

No matter how well the management system prescribed by the UNGPs is implemented by investors or the businesses, that they are directly linked to, actual adverse impacts will continue to occur. Investors are, per definition, responsible for all such impacts. This guide seeks to describe HOW investors meet the responsibility for seeking to prevent adverse impacts, that they are directly linked to through their investments, before the impacts occur (ex ante), and how investors meet their responsibility after the impacts have occurred (ex post).

When investors are made aware of severe 'actual adverse impacts' anywhere in their value chain the UNGPs expect investors to act; using their leverage and, if inadequate, building leverage to address the adverse impact. Thus, investors need to assure themselves that beneficiary companies have implemented the UNGPs.

This guidance outlines how investors can put in place a system to align their ESG practices with the UNGPs.

1.1 Is it necessary? – are investors also bound by the UNGPs

In 2013 the Thun Group of Banks questioned, whether financial institutions were bound by the UNGPs. The UN High Commissioner for Human Rights made clear to the group that not only are investors themselves

businesses, that need to meet the standard, and that they are directly linked to all the business activities, that they invest in.

Interestingly, the UNGPs can bring a much-needed focus and coherence to the field of ESG. The UNGPs represent the first globally agreed standard for responsible business conduct. The UNGPs describe a 'governance' system in addition to more traditional corporate governance issues, such as remuneration and conflict of interest (which inform expectations under the 'G' in ESG). However, the most obvious application to the ESG work would be to allow the UNGPs to enlighten investors' expectations under the S of ESG.

Basing ESG practices on the minimum standard will:

- enable an authoritative reference point
- avoid self-invented criteria
- enable comparability between investments
- scale up responsible business conduct globally

The UNGPs define respect for human rights by the establishment of key elements for a corporate governance system; all in alignment with the Governance criteria in ESG. The UNGPs designed governance system will enable both investors and the companies linked to the investors manage all relevant social risks; i.e. covering the S in ESG. The UNGPs principle 12 references the International Bill of Human Rights[1] as minimum scope for the management system, thereby ensuring that all elements of importance to human dignity are considered.

The Triple Bottom Line and the OECD Guidelines for Multinational Enterprises

The UNGPs define respect for human rights through a management system. However, the UNGPs management system was very similar to existing good practice management systems for environmental impacts and due diligence on anti-corruption; e.g., as recommended under the UK anti-bribery act. Hence the management system can be applied to the triple bottom line for sustainable development. In 2011, the OECD, on recommendation from late Prof. John Ruggie, incorporated, per verbum, the UNGPs management system into the OECD Guidelines for Multinational Enterprises; and applied it to the triple bottom line. The management system introduced by the UNGPs can thus be applied on the triple bottom line to manage all impacts under ESG: environmental areas (as established in both the Rio declaration on environmental sustainability and the Paris agreement on Climate Action), key social areas (International Bill of Human Rights, including core labour rights), and economic sustainability areas (at minimum the element mentioned in the UN Convention against Corruption, but also anti-trust and tax avoidance.).

[1] Please note that the International Covenant on Economic, Social, and Cultural Rights explicitly includes the five core labour rights that are included in the ILO Declaration on Fundamental Rights at Work

1.2 Limitation of the guide

Several guides have been developed to assist companies establish the management system required by the UNGPs[2].

This guide will not elaborate in detail, what can be expected from investors in terms of managing the potential and actual adverse impacts, that the investor, as any other company, may cause or contribute to (confer UNGPs Foundational Principle 13 a)[3].

UNGPs Foundational Principle 13

The responsibility requires businesses to:

a. **Avoid causing or contributing to adverse human rights impacts through their own activities, and address such impacts when they occur;**
b. **Seek to prevent or mitigate adverse human rights impacts that are directly linked to their operations, products or services by their business relationships, even if they have not contributed to those impacts.**

The limitation also means that the guide will not provide guidance to how investors should manage adverse impacts that they may cause or contribute to through their decisions or requirements to others.

An example could be that an investor requires a company to reduce its variable costs by 10 per cent within a year, as a condition for receiving a needed capital injection. It should be obvious, that the investor may contribute to adverse impacts on the right work (and possibly other human rights). A wider range of adverse impacts may well become the result of decisions that an investor with a majority stake in a company or project may have; e.g., by making the strategic decision to develop new products, digital solutions, or selling existing products in new geographical areas.

Investors should acknowledge that there are three distinct ways in which, they may be involved with adverse human rights impacts. Investors may 'cause', 'contribute to', or be 'linked to' adverse impacts.

In a letter to the Thun Group of Banks[4], Prof. John Ruggie, the author of the UNGPs, made it clear that there is a continuum between, when investors are merely linked to and when investors contribute to adverse impacts.

Financing a company that notoriously causes or contributes to severe impacts on human rights, but does not manage such risks of impacts, may bring the investor into a situation, where the involvement could be considered as 'contributing to' the impacts. Prof. John Ruggie wrote:

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[2] E.g., the GLOBAL CSR 'Primer' to the international minimum standard for responsible business conduct: https://globalcsr.net/wp-content/uploads/2019/02/23_GLOBAL_CSR_-Primer_Minimum_Standard_2205.pdf
[3] As reaffirmed by the UN Working Group, 12. July 2023: https://www.ohchr.org/sites/default/files/documents/issues/business/workinggroupbusiness/Statement-Financial-Sector-WG-business-12July2023.pdf - accessed 24.09.2023
[4] See: https://www.business-humanrights.org/sites/default/files/documents/Thun%20Final.pdf – accessed 20.09.2023

"There is a continuum between contribution and linkage. A variety of factors can determine where on that continuum a particular instance may sit. They include 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."[5]

1.3 Preliminary clarifications

1.3.1 Remediation and enabling access to remedy.

The UNGPs clearly states that businesses, and thereby investors, in situations, where they are *merely linked to* adverse impacts on human rights, are not expected to provide access to remedy for impacted persons.

investors may participate in the remediation, but it is not a requirement. Investors will in most instances merely be linked to adverse impacts through their investments. Hence this guide will not provide further guidance on how to remediate actual adverse impacts or establish effective grievance mechanisms. For more on access to remedy, see UNGPs principles 22 and 31.

1.3.2 Ex Ante and Ex Post

What is the minimum we can expect from investors, when managing their investments in businesses or projects run by businesses?

The UNGPs will require investors to: *"Seek to prevent or mitigate adverse human rights impacts that are directly linked to their operations, products or services by their business relationships, even if they have not contributed to those impacts"* (confer UNGPs Foundational principle 13 b.)

As the case would be with any other business, investors are well advised to design their ESG management systems in value chains with a distinction between processes, that are applied BEFORE an adverse impact occurs (ex ante), and AFTER an adverse impact has occurred (ex post) with a business relationship.

1.3.3 Prevention is better than cure

The intention of the UNGPs is that businesses deal with risks of adverse impacts on human rights before actual adverse impacts occur and before unmanaged adverse impacts escalate to become 'severe[6]' impacts. For an investor, escalations (i.e., ill-managed risks) may lead to situations that can disrupt the business operations jeopardizing the investment.

Investors should appreciate, that the UNGPs constitute a systems approach to proactive, rather than reactive, management of risks of human rights impacts.

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[5] See footnote 2 – p.2 – see also Prof. John Ruggie's letter to the OECD working party: https://www.business-humanrights.org/sites/default/files/documents/OECD%20Workshop%20Ruggie%20letter%20-%20Mar%202017%20v2.pdf - accessed 20.09.2023

[6] Severe impacts are also referred to as 'principal impacts', 'salient impacts', 'material impacts', 'significant impacts', etc. by various actors and regulation.

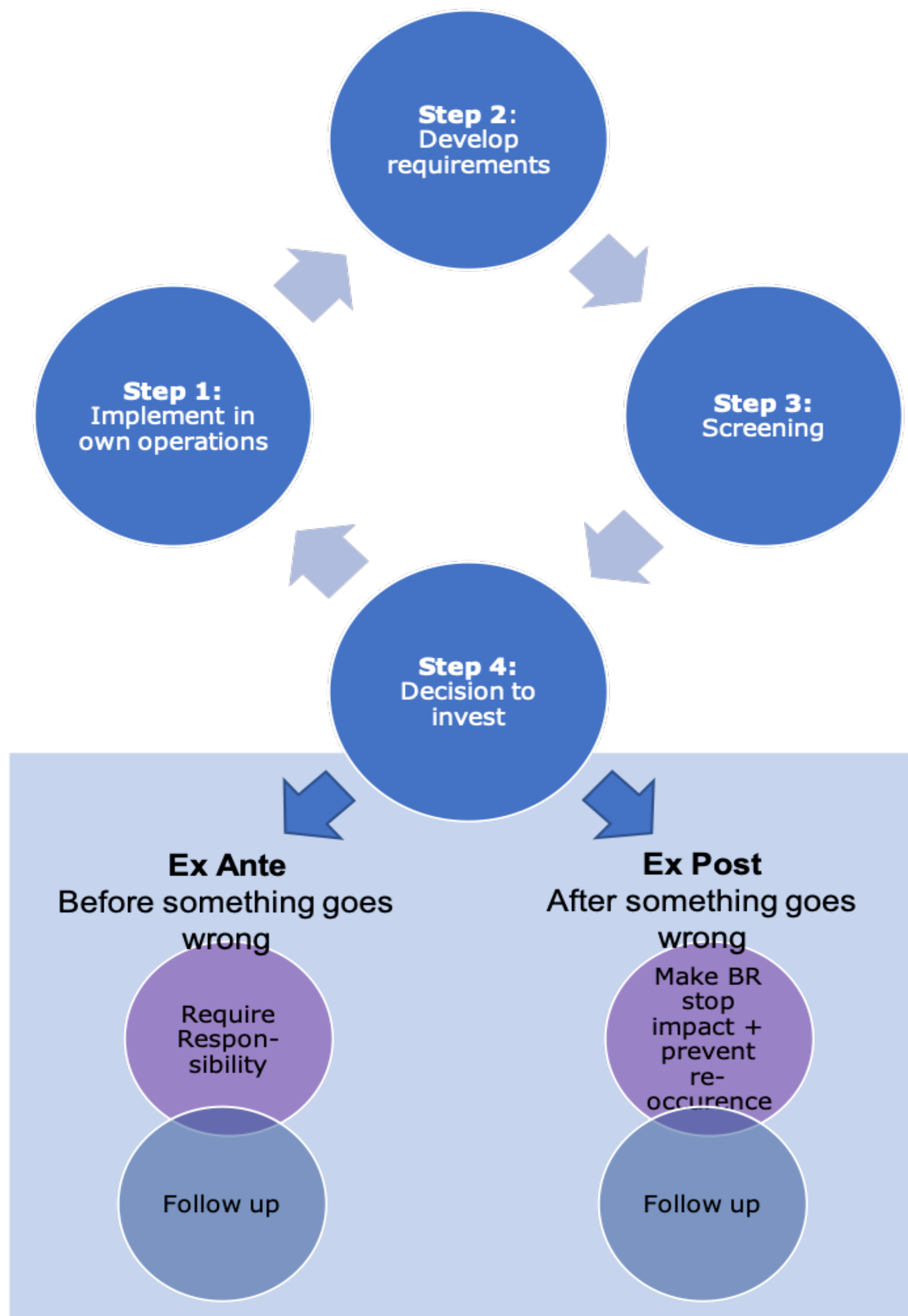
Illustration of proactive approaches managing adverse impacts on a specific human right:
Most businesses are well acquainted with establishing management systems to deal with risks of adverse impacts on the 'right to safe and healthy working conditions' (confer the ICESCR article 7). The more advanced companies apply a 'near miss' approach to the management system, where they engage and encourage employees to report incidences, that could have ended with adverse impacts on an employees' safety or health to ensure that risks are prevented before an accident occurs. This is the idea for addressing risks of adverse impacts on all parts of human dignity (i.e., all human rights) in alignment with the UNGPs; not merely one human right.

From an investor's perspective this intention of the UNGPs means, that the investor should emphasize the establishment of functional UNGPs aligned processes with the beneficiaries for the 'ex ante' situation; i.e., before actual severe adverse impacts have occurred or will occur with business relationships.

2. Embedding Responsibility with Investors

Below is a model on how to embed processes to ensure responsible investments in alignment with the UNGPs as described in this guide.

The model follows the chapters of the guide and illustrates an investor's responsibility before investments are made (blue circles) and after investments are made (blue square).



2.1 Before Investing

Step 1: Implementing in own operations

"UNGPs Foundational Principle 15:
In order to meet their responsibility to respect human rights, business enterprises should have in place policies and processes appropriate to their size and circumstances, including:

a) *A policy commitment to meet their responsibility to respect human rights;*
b) *A human rights due diligence process to identify, prevent, mitigate, and account for how they address their impacts on human rights;*
c) *Processes to enable the remediation of any adverse human rights impacts they cause or to which they contribute."*

Investors shall respect human rights. First step is committing to respect human rights through a policy (aligning with the key requirements in UNGPs principle 16). One of the requirements to a policy commitment is, that it explicitly describes expectations to business relationships. The minimum expectation to business relationships should be, that business relationships implement the UNGPs.[7]

The investor shall also conduct human rights due diligence. This involves identifying and managing risks of causing potential and actual adverse impacts or of contributing to adverse impacts as any other business entity in the world; e.g., preventing or mitigating the risk of adverse impacts on the right to rest and leisure, by making sure that overwork is managed well (confer UNGPs Foundational Principle 13 a)).

It also involves seeking to prevent or mitigate adverse impacts that the investor is directly linked to - i.e., the focus of this guide (confer UNGPs Foundational Principle 13 b)).

Finally, investors need to establish or participate in establishing grievance mechanisms to enable remedy for the people that experience actual adverse impacts that an investor causes or contributes to.

Hence, the investor shall implement the UNGPs in own operations; developing and approving a Policy Commitment, conducting due diligence through regular operational-level impact assessments, and providing access to remedy through effective grievance mechanisms.

Practise what you preach.
Investors can benefit from 'practicing what they preach'. If an investor can document to the companies the investor is linked to, how the investor meets its responsibility to respect human rights, it may guide the beneficiary company on how to meet the standard by example.

[7] An example of a sustainability commitment that is aligned with the UNGP scan be found at: https://polarisequity.dk/wp-content/uploads/2021/03/Polaris-Sustainability-Commitment-2021.pdf

Step 2: Develop Requirements

To begin work with responsible investments, investors should develop documents to assist sharing requirements with investments.

Most investments in publicly traded shares happen without any communication between the investor and the company. However, the expectation can be expressed through the public communication of the investor to the market and public in general, such as through the Policy Commitment (Step 1), and during participation in investor meetings that the listed companies invite for, when promoting investments in their shares.

When an investor participates in an initial public offering (IPO), the requirement to meet the standard for the company in question shall be levied at an early stage. It should only be a matter of time before stock exchanges around the world will apply the minimum standard for responsible business conduct to the minimum criteria of accepting stocks for trade. However, until this happens, the investor may pose the requirement.

Sustainability Indices

Over the years, numerous indices have emerged to assist investors benchmark publicly listed companies against each other; e.g., the Dow Jones Sustainability Indices; the FTSE4Good Index Series; the STOXX® Global ESG Leaders index; the Ethibel series; the MSCI ACWI ESG Leaders Index; etc. Whereas human rights may feature as an issue, or a few specific human rights may be mentioned, none of the indices reviewed align with the UNGPs yet. One attempt to create an index, confer the Corporate Human Rights Benchmark represents a step forward. However, both content and methodology could possibly benefit from aligning better with the UN Guiding Principles Reporting Framework prepared by SHIFT and Mazar. Investors can assist in further enabling the use of the global minimum standard thereby minimizing the confusion created by the multifarious indices and their somewhat arbitrary measuring points. Interestingly, even contemporary UN initiatives relating to finance and investments appears to miss references and application of the minimum standard, confer e.g., the UNEP FI Principles for Responsible Banking and The Taskforce on Nature-related Financial Disclosures (TNFD).

Investors that seek to align their requirements on ESG with the UNGPs/OECD will continuously meet increased appreciation by the beneficiaries when ESG related regulations are passed by nation states. In the EU regulation based on the UNGPs/OECD is massive during recent years.

ESG/Sustainability Regulation in the EU
When the EU in 2014 incorporated the UNGPs into the non-financial reporting requirements through directives, the intention was to make larger companies and financial institutions in the EU aware of the standard; to create a common reference point and a level playing field. Investors are the primary beneficiaries of such annual reporting. With the recent increased focus on sustainable development and the EU 'green deal', the EU steps up its implementation efforts of the UNGPs. In the EU Taxonomy Regulation, 2020, it is required that any company participating in a 'green investment', shall meet the 'minimum safeguards' that are defined as the UNGPs/OECD, confer Art. 18. The Corporate Sustainability Reporting Directive (CSRD), 2023, is explicitly based on the UNGPs/OECD. Article 19 a, sect. 2, outlining the reporting requirements of companies, is aligned with the management processes defined by the UNGPs and copied into the OECD Guidelines. Implementation of the UNGPs/OECD due diligence requirements are considered a prerequisite and eases considerably meeting the reporting requirements. The Delegated Act authorised by the Directive contains the European Sustainability Reporting Standards (ESRS), i.e., the concrete KPIs whereby the directive seeks improve comparability and align reporting across the EU. The sole mandatory ESRS mandates companies to report on their implementation of the UNGPs/OECD, whereas the additional ESRS provide datapoints for a limited subset of sustainability areas, to be applied should the company in question identify risks of 'material', i.e., severe, impacts in this area. The Corporate Sustainability Due Diligence Directive (CSDDD), expected to be adopted in late 2023, in its first draft referred explicitly to the UNGPs/OECD as the foundation for the directive. The requirement to implement, and hence document due diligence, shall be enforced by legal liability in the form of fines for non-compliance. The fines shall be persuasive and proportional to the turnover like the mechanism known from GDPR. In addition, the draft went beyond the definitions contained in the UNGPs and introduced possible civil liability for impacts occurring in the value chain. From an attorney's point of view such proposed deviation from the definitions in the UNGPs can create immense legal and judicial challenges. Finally, the Digital Services Act (Regulation (EU) 2022/2065, DSA), has introduced human rights due diligence, requiring digital services providers in the EU to assess potential adverse impacts on fundamental rights, e.g., in the design of the algorithmic systems used by the very large online platforms or search engines, in relation to the misuse of their service design of online interfaces. This legal requirement has not gained much attention in ESG circles, possibly due to fact that few companies know, what 'documenting' human rights due diligence require.

Non-listed shares
Investments in non-listed share may happen directly or through a fund manager. In both instances a basic requirement to the beneficiary company should be that the company in question 'respects human rights'. In addition to stating this requirement in your policy commitment, a Code of Conduct for Business Relationships (CoCBR) can further explain the key elements of the required management system to your business relationships.

A Code of Conduct for Business Relationships[8] should include:

- A requirement to beneficiaries, that they implement the global minimum standard for responsible business conduct: The UNGPs and can document implementation. Documentation includes a policy commitment approved at the highest governance level, human rights due diligence documented through operational level impact assessments in own operations and sharing the requirement with their business relationships, in addition to using or building leverage with entities in the value chain that cause or contribute to severe impacts, and the establishment of effective grievance mechanisms.
- A requirement that they escalate information to the investor about their management of actual *severe* adverse impacts that they cause or contribute to or that they are linked to.
- Expectations for a timeline; i.e., if a business has not yet implemented the UNGPs, a realistic timeframe to adopt their policy commitment and conduct their first operational-level human rights impact assessments should be provided.
- Information that if an investment does not show willingness to implement the standard or neglects to escalate information about severe adverse impacts to the investor, it may be considered material breach under the agreement.

Requirements can be embedded in contract clauses in investment contracts, referencing the CoCBR. A contract clause can tie the requirements directly to other default clauses governing the investment. The UNGPs explicitly recognise that a contract clause can improve your leverage as an investor should the beneficiary company become involved with severe human rights impacts; confer UNGPs 19 (b) (ii) and the interpretative guide[9].

Sharing requirements as minority and majority shareholders
Investors with minority shares may experience that they have less leverage on how responsibility is managed in investments. Investors should still share their requirement with any business relationship, including beneficiary companies. In cases where other investors put forward non-aligned industry or even self-invented ESG/SRI standards, an investor aligning with the UNGPs can benefit from sharing information on their expectations with other shareholders. This may encourage positive collaboration on enhancing implementation of the UNGPs. For all investors it is better to develop and share expectations for beneficiaries to meet the UNGPs as early as possible. This will smoothen and assist the process of managing investments responsibly; and meeting existing and coming legal requirements.

Sharing requirements as asset owners and managers
Both asset owners and managers should put forward similar requirements for their responsible investments. Asset owners should require from managers, that assets are managed in line with the UNGPs. This means that at minimum, the asset manager implements the UNGPs to manage their business, and investments, responsibly.

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[8] The GLOBAL CSR Code of Conduct for Business Relationships can be found at: https://globalcsr.net/wp-content/uploads/2019/02/21_GLOBAL_CSR_CoC_BR_1902.pdf
[9] See https://www.ohchr.org/sites/default/files/Documents/publications/hr.puB.12.2_en.pdf - accessed 23 September 2023

Asset managers should share with asset owners the expectations they put forward to beneficiary companies and incentivise positive collaboration with asset owners on the UNGPs. Asset managers should require beneficiary companies to implement the management system of the UNGPs during ownership.

Step 3: Screening procedure

Screening procedures in alignment with the UNGPs should focus on examining the degree to which potential investments' (beneficiaries') processes and procedures on responsible business conduct align with the UNGPs. An investor may screen for severe issues in a potential investments' operations or history. However, not looking for procedures to identify and manage risks, will leave the investor with an inadequate overview of how well a potential business relationship knows and manages its risks. Merely looking for issues can often misguide investors, leading them to invest in a company that at the outset does not seem to have many risks (issues), but may turn out to have severe issues related to impacts on the human rights of employees or other stakeholders.

Screening for procedures thus makes it possible to develop a more nuanced picture of potential investments. It helps investors know how well they can trust that risks are managed adequately by potential relationships. Thus, rather than trying to predict the issues some businesses or projects may have depending on their products or location, investors can get valuable information about, how well such businesses are already identifying and managing their risks. To ensure a screening procedure focused on processes and procedures, an investor should ask to alignment with the UNGPs:

- Does the beneficiary have a policy commitment in place, and does it meet the requirements from the UNGPs?
- Does the beneficiary have a due diligence process in place, and can it share operational-level impact assessments covering all human rights with investors?
- Does the beneficiary require from its business relationships to meet the globally agreed minimum standard? (or does it merely ask one end of the value chain, typically suppliers, to meet pre-defined and self-invented standards on a few labour rights)
- Does the beneficiary have effective, operational-level grievance mechanisms in place to provide access to remedy to potentially impacted stakeholders?

Screening as minority and majority shareholders

Screening procedures will be the same for investors with minority or majority shares. However, the results from a screening may encourage different actions depending on whether an investor is planning to become a minority or majority shareholder. For more on this, see also Step 4 on deciding and evaluating.

Screening as an asset owner or manager

As an asset manager, screening of risk management procedures on human rights is important to get an overview of the status of a potential beneficiary's responsible business conduct. This includes the level of risk the beneficiary may pose to the investor, conditions to get an idea of the costs expected related to implementation, and the level of trust a business can have in a potential beneficiary's management of social, i.e., human rights, risks.

Asset owners will rarely screen beneficiaries themselves. However, if asset owners do have screening procedures in place both in relation to potential and existing beneficiaries, they should align such procedures to examine the level of implementation of the UNGPs.

Asset owners should further ensure that those responsible for managing their investments have adequate screening procedures in place, ensuring that the risk pattern identified adequately reflects the potential beneficiary's management of risks, thus not providing imprecise risk assessments for the asset owner.

Step 4: Decision to invest and evaluating opportunities for improvement
Potential investments should be able to show that they meet the minimum standard for responsible business conduct, as this is a global requirement for all businesses in the world. However, States have reacted to their duty to regulate businesses within their territory to respect human rights in recent years only, and the UNGPs are still in their early stages of implementation by a small fraction of businesses. Hence, few potential investments would be able to demonstrate adequate implementation of the UNGPs, if any.

Thus oftentimes, investments will be made in companies or projects, that did not yet align with the global minimum standard. At this point of time, investors should not avoid investing due to lacking alignment with the UNGPs per se. However, knowing the level of implementation, or a potential beneficiary's stance on responsible business conduct, can help predict the efforts that will be necessary for changing conduct to align, and minimise the risks to both social sustainability and to the financial return.

The investor may consider that the beneficiary or the project will have a range of un-detected and un-managed risks and may estimate the costs related to implementing the UNGPs following the investment, when negotiating the valuation. In addition, the lack of implementation of the globally agreed minimum standard for responsible business conduct will provide the investor with an indication of the capacity of the leadership of the company. In the event of major investment, the investor, should assess the willingness of the continuing leaderships to align their ESG approach with the UNGPs.

Questions to pose before investment:
The decision to invest in companies that do not yet meet the standard should be informed by the following questions:

- Is the investor willing to carry the heightened risk by investing in a business or project that most likely have unidentified and unmanaged risks, until implementation has happened?
- Is the company or project willing to implement the UNGPs within an agreed timeframe?
- Will the investor have enough leverage, or can the investor build leverage without extensive efforts, to make the company implement the UNGPs?
- Does the cost reflect the expected expenses by improving the management of risks in the company?
- Is the management, that ignored the UNGPs, the best suitable management of the company or project?

2.2 After Investing

A: Ex Ante

The UNGPs make special mentioning of investors. When describing the requirement of a company to be able to communicate the results of due diligence, (i.e., what the company identified, what it does to prevent or mitigate the risks of adverse impacts, and how it measures effectiveness of the actions) to – at minimum - the potentially impacted people and the company's business relationships.

The UNGPs explicitly mentions that the company will have to disclose this information to its investors.

> **UNGPs operational principle 21, commentary:**
> *"The responsibility to respect human rights requires that business enterprises have in place policies and processes through which they can both know and show that they respect human rights in practice. Showing involves communication, providing a measure of transparency and accountability to individuals or groups who may be impacted and to other relevant stakeholders, including investors."*

When the investor has decided to go along with the investment and posed the requirement that the beneficiary implements the UNGPs**,** the investor should manage and follow up on this requirement. Some investors have positions, and shift positions, in so many companies or projects that it would be virtually impossible to engage all the companies that the investor is linked to.

Nevertheless, for the responsible investor it is a fair requirement to expect the beneficiary company to meet the globally agreed minimum standard for responsible business conduct. If fulfilled, the beneficiary company should be able to document how far it is in meeting and maintaining the management system upon request from the investor; and the results of the latest operational-level impact assessments.

Where an investor acquires a majority stake or controlling influence in a beneficiary company, the investor has the responsibility to ensure that the beneficiary company, that is now a subsidiary, meets the standard.

Where the investments do not create controlling stakes, the investor should, in addition to expecting implementation from all investments, engage with a few chosen investments to collaborate in enabling responsible business conduct. The investor should be transparent about the criteria that the investor applies in determining, where the investor will use the extra resources to engage. The investor shall, at a minimum, engage, when known severe impacts occur with the company.

In alignment with this, the Principles for Responsible Investment (PRI), long before the UNGPs were endorsed, established that investors should demonstrate active ownership, confer principle 2: "*We will be active owners and incorporate ESG issues into our ownership policies and practices"*.[10] In practice, active

[10] See https://www.unpri.org/about-us/what-are-the-principles-for-responsible-investment - accessed 11 October 2023

ownership has primarily targeted ex post situations, see below. However, investors that commit to PRI also commit to: "*Develop an engagement capability (either directly or through outsourcing).*"

The first, and inevitable, criteria should centre around "known risks of severe impacts". If the beneficiary company has a history of severe impacts, or due to the nature of the company's operations or operating context are exposed to increased risks for severe adverse human rights impacts, it will be expected that the investor engages with the company.

Another criterium could be dependency. If the investor is depending on an investment in a beneficiary company, it should be vital for the investor to ensure that the beneficiary company meets the minimum standard. The beneficiary company will be considered 'crucial' to the investor, using the terminology applied by the UNGPs. If dependent, the investor cannot sell the assets should the beneficiary company become involved with severe impacts due to lack of proper human rights due diligence. Hence, unmanaged human rights risks will continue to be a risk for the investor; and even worse the investor cannot escape its connection to such severe impacts.

Further criteria to decide, which investments to engage with, could be the size of an investment. Where the investor has large investments in beneficiary companies or projects, the likelihood of being exposed for such linkages, should severe impacts occur, are greater. While the UNGPs explicitly require businesses to establish the required management systems with focus on the severity of the impact to people and not with a focus on the (reputational) risks to the businesses, the criterium can be applied next to 'known risks': Also confer the box below on 'Materiality'.

Materiality – and double materiality

Investors need to create financial revenue from their investments. Any risks of occurrences that can harm the prospects of a proper return of investment should be managed. In traditional ESG management, financial risks would be assessed to determine, whether ESG risks are 'financially material' or not. For public funds such 'financially material' risks and their mitigation would require public communication. This discourse evolved from the stakeholder-based approach to responsible business conduct; which 'issues', that were identified through stakeholder engagement, would be assessed financially material to the company. The company's ESG or Corporate Responsibility strategies would address the 'financially material' issues; i.e., a fraction of the issues identified by the company's stakeholders. Material issues would be those that could cause material financial harm to the company. The UNGPs human rights due diligence process centres around potential harm to the impacted person(s) and not to the company. Unmanaged severe human rights impacts may often create a 'financially material' issue for the company and may therefore become included in the ESG/CR strategy of the company. However, if the impacted person(s) is/are vulnerable or otherwise disempowered, they may not have a voice. Hence, the impact would not be considered a 'financial material' risk to the company. With the UNGPs, investors that apply 'materiality' to their ESG/CR work, should, a priori, consider the implementation of the UNGPs as material. For EU companies the introduction of 'double materiality' reflects that the Corporate Sustainability Reporting Directive is based on the UNGPs/OECD. Companies shall report on severe (material) impacts, whether they are financially material or not. Reversely, it is difficult to construct an example of 'financially material' issues, that would not have been identified as a risk of severe (material) impacts during the sustainability due diligence process, as outlined by the UNGPs/OECD.

B: Ex Post

After (severe) impacts have occurred with investments.

It is the investors responsibility to seek to prevent and mitigate adverse impacts with investments, confer UNGPs Foundational Principle 13 b). When an investor is informed about actual severe adverse impacts with an investment, measures should be taken to manage concrete issues or situations *after something has gone wrong,* in alignment with the UNGPs.

Severity parameters:
SCALE: the weight of the impact (e.g., forced labour; exploitative child labor etc.)
SCOPE: the amount of people affected by the impact (e.g., serving poisonous food; selling tobacco)
IRREMEDIABILITY: Can the impact be remediated? (e.g., death or chronic injuries)

Managing impacts with investments after they have occurred, is distinct from *preventive work to ensure due diligence with investments*. Responsibility before something goes wrong is described in the above section A.

An investor may be made aware of the challenges through reports or in public media, or when visiting an investment. Other business relationships may also make the investor aware of challenges.

WHO SHOULD BE INVOLVED?
Is it a journalist or an NGO that contact the investor about an actual severe human rights impact that is caused or contributed to by a business relationship of the investor, the investor should refer the matter to management or a communications department. When managing the issue, collaborate with management or the communications department, involving the subject matter specialists that know the UNGPs well.

REMEMBER
Be accommodating to any criticism. All companies are at risk of causing or contributing to severe human rights adverse impacts, and all companies are responsible for adverse impacts in their full value chain. No one can deny this responsibility. Appreciate the information, investigate the issue and manage it.

When an impact occurs that the investor is directly linked to, an investor should use its leverage to make the impact stop and not reoccur. Leverage is considered to exist, where the investor can effect change in the wrongful practices of the entity that causes or contributes to the harm. Leverage can be established in many ways, and if the investor finds that it has no leverage, i.e., cannot effect change in behaviour by the beneficiary company, the investor should seek to build leverage. One way of establishing leverage from the outset could be to reflect the requirements outlined in the Code of Conduct for Business Relationships in the contract clauses in the agreement between the investor and the beneficiary company.

Rule of thumb: Any contact from the press or NGO's can be assumed to be about actual *severe adverse human rights impacts*, whereas conditions that colleagues may notice, can be about less severe adverse impacts. In the latter case, an investor may mention the issue to the investment, but one should assume that the investment will manage the issue as it establishes its human rights due diligence system and become transparent about the results, i.e., what it does to prevent or mitigate the impact and how it measures the effectiveness of such actions.

Evaluation of leverage

Leverage is evaluated from the following criteria[11]:

1. Does the investor have any direct control over the causing or contributing entity?
2. Does the investor have a contract with an ESG/CR clause with the causing or contributing entity?
3. Is the investor a big or important investor to beneficiary company?
4. Can the investor establish positive incentives, promoting the causing or contributing entity's motivation to improve the situation?
5. Would ending the relationship impact the reputation of the causing or contributing entity?
6. Can the investor collaborate with other investors, business relationships, or industry associations of importance to the causing or contributing entity to increase leverage?
7. Can the investor engage local, central or multilateral public institutions, to increase leverage and have the causing or contributing entity act?

Criteria 1-5 can inform the investor of the leverage it may already have towards the causing or contributing entity. Criteria 6-7 can inform the investor of the immediate possibility to increase leverage in cases where it does not have leverage.

Crucial investments

It is rare that investments may be deemed crucial to an investor. An income decrease as a result of a sale will not be deemed crucial, unless it can seriously threaten the economic position of the investor. If the relationship is crucial, the requirements to manage the issue will become more critical, as the investor will not be able to end the relationship.

Choosing action

Depending on an investor's leverage with the beneficiary company, and how crucial the investment in question is, the investor should choose the appropriate reaction from four possible when severe impacts occur with the beneficiary company[12]:

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[11]The UN SRSG, Prof. John Ruggie, outlined the criteria for leverage in 2010 in a response to the OECD on how to address adverse impacts on human rights with business relationships – see: http://www.oecd.org/daf/inv/mne/45535896.pdf - accessed 20.9.2023

[12] The figure builds on the similar figure created by the UN SRSG, Prof. John Ruggie, in 2010 in a response to the OECD on how to address adverse impacts on human rights with business relationships(confer footnote 11) with additions that came as a result of a report that GLOBAL CSR wrote for the Danish Ministry of Business and Growth and the Danish Shipowners Association in 2013 on how to apply the UNGPs to responsible supply chain management, where the draft was graciously reviewed and commented upon by Prof. john Ruggie. Unfortunately, the report was not made public.

	Have sufficient leverage	Lack sufficient leverage
Crucial investment	**Reaction 1** Use leverage to make the causing or contributing entity stop the adverse impact and prevent or mitigate reoccurrences. If the investor does not succeed, re-examine leverage: go to Reaction 2.	**Reaction 2** Take concrete measures to build the leverage needed to see change with the causing or contributing entity. If sufficient leverage is built: Go to Reaction 1. If the investor does not succeed: As it is a crucial investment, the investor might be forced to continue the relationship. In this case the investor should, at a minimum, be able to demonstrate continuous efforts to build leverage.
Less crucial investment	**Reaction 3** Use leverage to make the causing or contributing entity stop the adverse impact and prevent or mitigate reoccurrences. If the investor does not succeed, re-examine leverage: go to Reaction 4.	**Reaction 4** Evaluate opportunities to build leverage. If the investor can build sufficient leverage, go to Reaction 3. If the investor can't build sufficient leverage, the investor should end the relationship. Be aware of risks of adverse impacts or worsening the situation from ending a relationship.

Collaborating

If an investor has or can build sufficient leverage with an investment, the investor should collaborate with the causing or contributing entity to make sure that they stop the impact and prevent or mitigate future reoccurrences. Effective collaboration could look like:

1. Ask the entity to stop the specific adverse impact, measure effectiveness of their actions and communicate the results back to the investor before a given deadline.
2. Establish constructive dialogue by following up on the received information.
   Has the impact stopped? Continue collaboration.
   Has the impact not yet been stopped? Evaluate whether this can be changed by increasing communication, giving a more realistic deadline, or seek to increase leverage to ensure that the impact is stopped.

It is not necessary to visit a site where severe impacts occur, even in case of severe impacts. It may however have a positive effect on the collaboration in some cases. If the investor evaluates that it can be helpful to visit the causing or contributing entity, such a visit will be optimal between action 2 and 3. This is the time where advice can best assist implementation of adequate actions.

3. Collaborate on establishing a UNGPs aligned human rights due diligence processes with the causing or contributing entity. This can be done by sharing good practice, including by sharing information on necessary steps to implement the management system, the approach the investor has taken, and by showing the results from own processes, including: Policy commitments, latest impact assessments, Codes of Conduct, etc.
4. Maintain an ongoing dialogue until it is no longer deemed likely that the adverse impact continues or reoccurs; and adequate human rights due diligence processes are established to demonstrate responsible business conduct.

Follow up with the causing or contributing entity also after an impact is stopped and this process is ended, to evaluate whether the business relationship is managing its responsibility, hereunder risks of reoccurrences, effectively – in alignment with the standard (UNGPs).

If faced with multiple challenges and lacking resources to manage them all, investors should use the severity parameters to decide, what challenges should be managed first.

Management of severe impacts should, following the global standard and to the degree possible, be made public as part of the investors efforts to demonstrate responsible business conduct. It is generally a good idea to design and undertake actions in consideration of what can withstand publicity.

3. Overview of Due Diligence Process

When an investor has fully embedded the UNGPs in its practices, its due diligence processes could be illustrated as outlined in the figure below. The investor's responsibility before specific adverse impacts occur in its value chain, consists of ensuring appropriate screening procedures for responsible management, influencing decisions on investments. Upon investing, the investor should require all investments to align with the UNGPs. Finally, the investor should follow up where possible, to ensure implementation. If something goes wrong, and an investor is made aware of an actual severe adverse human rights impact that it is linked to, the investor must use or build its leverage to make the causing or contributing entity stop the impact and prevent re-occurrence. When the impact has stopped, the investor should follow up to ensure that effective due diligence procedures are in place to prevent or mitigate reoccurrences.