Call for Input on 'Development Finance Institutions and Human Rights', Working Group on the Issue of Human Rights and Transnational Corporations and Other Business Enterprises, UN Human Rights Council

Submission by researchers on the New Frontiers in International Development Finance (NeF DeF) project

The NeF DeF project brings together research and policy thinking on how the shifting landscape of international development finance impacts on law, regulation and governance. Our focus is to map, assess and critique this evolving architecture and what this means for international development cooperation and global economic governance. Our work seeks to engage in an interdisciplinary examination of these changes in international development finance policy and practice, drawing from insights from a range of disciplines including law, politics, economics and finance, sociology and geography.

Our publications from which this report draws on can be found on our website: http://go.warwick.ac.uk/nefdef

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It draws on the work of NeF DeF researchers which can be found here.

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We welcome the initiative of the Working Group on the issue of human rights and transnational corporations and other business enterprises ('Working Group') to present a report to the Human Rights Council at its 53rd session in June 2023 on 'Development Finance Institutions and Human Rights'. We commend the UN Working Group's initiative to guide states, development finance institutions (DFIs), and other stakeholders on practical aspects in efforts to strengthen protection and respect for human rights through development financing that adheres to the UN Guiding Principles on Business and Human Rights and invite the Working Group to also address international human rights and environmental law obligations more broadly, for instance, in tackling specific human rights or environmental challenges such as the rights of specific groups of persons more prone to marginalization by referencing specific instruments *inter alia* on women's rights, children's rights, the rights of persons with disabilities as well as obligations related to specific environmental issues such as the climate crisis, environmental pollution, biodiversity, among others.

As members of the New Frontiers in Development Finance (NeFDeF) international research collaboration, we would like to share some insights and comments with the Working Group. Our submission is informed by our research on the legal and policy architecture of sustainable development and climate finance in the context of greater engagement with private sector investment and finance in development.

DFIs have become central to the international community's mobilisation, disbursement and delivery of financing sustainable development as well as climate change mitigation and adaptation. Under the private finance agendas espoused by many development actors, DFIs have the institutional mandates and operational capacity to lend to and engage in partnerships with the private sector. This characteristic of DFIs and their hybrid public-private roles as investors and financiers make it imperative that they are subjected to greater scrutiny and accountability by national and international human rights laws and institutions.

The enhanced role of DFIs within this emerging public-private ecosystem of development and climate finance also calls for greater transparency, accountability and harmonisation of rules, standards and procedures for human rights and environmental safeguards in DFI-financed projects. Our research demonstrates that the rapid diversification and proliferation of financing platforms, including greater dispersal of official financing to private entities and public-private partnerships (PPPs), have fragmented and diluted the governance of development finance and undermined existing accountability and safeguards frameworks.[1]

Our submission centres on key messages in the context of the **State duty to protect human rights, including the duties of Home States of DFIs** as well as **DFIs' responsibility to respect human rights.**

1. Home State Duty to Protect Human Rights

[1] See Erdem Türkelli, Gamze (2022), 'Multistakeholder Partnerships for Development and the Financialization of Development Assistance', *Development and Change*, Vol 53, No 1; Tan, Celine (2021), 'Audit as Accountability: Technical Authority and Expertise in the Governance of Private Financing for Development', *Social and Legal Studies*, Vol 31, No 1; Tan, Celine (2019), 'Creative Cocktails or Toxic Brews? Blended Finance and the Regulatory Framework for Sustainable Development', in Gammage, C and Novitz, T (eds), *Sustainable Trade, Investment, and Finance: Toward Responsible and Coherent Regulatory Frameworks*, Edward Elgar.

In instances of development-induced human rights violations, such as forced displacement of local communities in DFI-financed projects, the bulk of the attention has traditionally been focused on host states of investment projects and the ability of their domestic legal and institutional framework to protect project-affected peoples. Host states are traditionally viewed as the primary duty bearers of human rights obligations in relation to development projects occurring within their own jurisdiction.

Less attention has been paid to the home countries of the DFIs and their responsibilities as investors and financiers of development projects. However, it is clear that the home states of DFIs have a duty to protect human rights, including by regulating and exercising oversight over the activities of state-owned or state-controlled DFIs, at the multilateral, regional or bilateral levels[2].

Many bilateral DFIs are established as corporations under national law that are fully or majority owned by home states. As such, they straddle two identities: (1) corporate legal forms that are governed by company law in domestic jurisdictions; (2) state-owned enterprises (SOEs) and/or state-controlled institutions that can be subject to domestic public administrative law. Additionally, DFIs will attract duties under the UN Guiding Principles on Business and Human Rights (UNGPs) under all three pillars: *protect*, *respect* and *remedy*.

In line with UNGP 4, home states of DFIs 'should take additional steps to protect against human rights abuses by business enterprises that are owned or controlled by the State, or that receive substantial support and services from State agencies such as export credit agencies and official investment insurance or guarantee agencies, including, where appropriate, by requiring human rights due diligence'. In addition, in line with UNGP 8, home states of DFIs should ensure that DFIs 'are aware of and observe the State's human rights obligations when fulfilling their respective mandates, including by providing them with relevant information, training and support'.

In many countries, DFIs are incorporated as companies with full or substantial shareholding of their home governments. For example, the Norwegian and Belgian governments are the only shareholders in Norfund and the Belgian Investment Company for developing Countries (BIO), respectively; while the government of the Netherlands is the largest shareholder of the shareholding in Dutch Entrepreneurial Development Bank (FMO). In the UK, the British International Investment (BII) is a public limited company that is wholly owned by the UK Government with the Foreign, Commonwealth and Development Organisation (FCDO) as its only shareholder.

As these DFIs advance the foreign development and cooperation policies of their home countries and are funded by partly or fully through official/ public resources, the home states have effective control over DFIs to be able to actively regulate them to ensure that the projects they finance and their investments abroad do not adversely affect the enjoyment of human rights in the host states and do not cause environmental damage.

Absence of adequate and effective regulation by the home states of DFIs exposes vulnerable groups like indigenous peoples, women, people with disabilities, children among others to further marginalization and to the risk of further impoverishment of their livelihood. In such instances, DFIs may make arbitrary determinations as to who they recognize as belonging to a particular vulnerable group, even if such a determination is in contravention to the existing normative human rights standards. For example, in the implementation of Lake Turkana Wind Power Project in Kenya (2006-

[2] UN OHCHR (2022), 'Benchmarking Study of Development Finance Institutions' Safeguard Policies', Consultation Draft, UN Office of the High Commissioner for Human Rights (OHCHR) 7 June 222.

2019), which was financed through several DFIs' blended concessional financing, the Project Company did not consider three of the affected communities including Samburu and Turkana peoples as indigenous communities despite the fact that the African Commission on Human and Peoples' Rights has recognized them as such.[3]

The existing economic power discrepancies between the DFIs' home countries and host countries, where the latter usually have low bargaining power, the livelihoods of the affected communities may be further impoverished by the implementation of development projects especially where there is weak domestic legal framework on involuntary resettlements in the host states if home states do not ensure that DFIs observe adequate and effective safeguards in project implementation.

2. DFIs' Responsibility to Respect Human Rights

Given the corporate identity of DFIs, in line with UNGPs, they have a responsibility to respect human rights. UNGP 11 requires business enterprises to do no harm and to address 'adverse human rights impacts with which they are involved'. In addition, UNGP 13(b) underscores that business enterprises should '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 these impacts'. These requirements squarely apply to DFIs which are involved in adverse human rights impacts as financiers.

Many DFIs have harmonized their policies with and still rely heavily on the non-binding the International Finance Corporation (IFC) Performance Standards on Environmental and Social Sustainability (2012). DFIs thus address possible human rights violations as identified 'social risks' and handle them as a matter of compliance and covered under the relevant management system with little regard to the resultant actual human rights violations. Research has demonstrated that even where host states have signed on to international legal obligations to provide meaningful consultation and consent processes, project agreements themselves can circumvent the accessibility of project information by project-affected peoples and create impediments to effective participation in consultative procedures. For example, there has been research to show that that despite the existence of IFC Performance Standards (including P7 on Indigenous Peoples) that guarantees free, prior and informant consent (FPIC), the standard may not be operationalised in reality.[4]

The Working Group should advise DFIs, which are legally established as state-owned enterprises or as corporations wholly owned by government agencies, to expressly outline in regulatory documents the binding nature of their human rights duties towards the people who may be directly or indirectly affected by their projects. As it stands, Codes of Conduct, Environmental and Social Sustainability Policies and Human Rights Statements and Guidance Notes do not provide express and binding obligations that the affected people can rely on in case of infringements.[5] Many of these internal corporate governance safeguards allow claims only for breaches of internal policies or failures of internal due diligence rather than broader, more substantive human rights norms. Consequently, in the event of complaints by affected people, DFIs and their clients can be found to have correctly complied with their environmental, social and governance (ESG) policies notwithstanding the effect of the implementation of the project on human rights of the affected people.

[3] Voller, L and Brønd Christensen, A (2016), 'A People in the Way of Progress', 30 May 2016.
[4] Bhatt, K (2020), *Concessionaires, Financiers and Communities: Implementing Indigenous Peoples' Rights to Land in Transnational Development Projects*, Cambridge University Press.
[5] UN OHCHR (2022), note 2 above.

Additionally, the Working Group should encourage greater harmonisation of standards that are in danger of being diluted through increased fragmentation of development finance and dispersal of such finance across a more disparate set of public and private actors. There is currently no harmonised framework for ensuring that these private investments meet common standards of environmental and social safeguards, including those contained in international legal instruments and non-binding standards, including the UNGPs and the OECD Guidelines for Multinational Corporations and the Principles for Responsible Investing. The widespread use of financial intermediaries, including by DFIs, in the disbursement of private finance for development also distances official financiers from the intended beneficiaries of the development projects, making it difficult to ensure safeguard policies and standards are upheld throughout the financing chain.[6]

3. Home states and DFIs Duties to Provide Remedy

The third pillar of the UN Framework and the UNGPs on remedy is a key component of accountability of DFIs to rights-holders. Both home states of DFIs and DFIs themselves have important roles to play in providing effective remedy to rights-holders. In line with UNGP 31, remedy mechanisms should be legitimate, accessible, predictable, equitable, transparent and above all, rights-compatible.

There is a need for external accountability and oversight of DFIs. At present, DFIs are largely self-regulated and operate in line with mandates that focus on creating impacts and generating returns for investments. This can result in DFIs being more accountable to their shareholders than the people adversely affected by their projects. As such, upon failure or successful completion of the project, the DFIs may exit notwithstanding the fact that the rights of the people adversely affected by the project remain unaddressed. For example, upon failure of the Addax Bioenergy Project in Sierra Leone in 2015, nine bilateral DFIs involved, among them FMO, BIO and German DFI exited the project upon payment regardless of the fact that local people who had been economically and physically displaced by the project were left in limbo with impoverished livelihoods and no form of recourse.[7]

Accountability becomes more challenging in a blended concessional finance where multilateral and bilateral DFIs, commercial lenders and other private financiers are involved. There is greater opacity surrounding private sector projects in development compared to those undertaken by the public sector through an official sector grant or loan (eg through an multilateral development bank as opposed to a DFI). DFIs and PPPs that lend to private entities as opposed to national or sub-national governments tend to have weaker transparency and information disclosure policies than their public counterparts on grounds of commercial sensitivity or client confidentiality .[8] Additionally, where development projects are structured through a PPP between the state and a private investor, it becomes apparent that the fragmented legal structure of PPP projects presents unique challenges for community participation and access to information, both at the pre-project consent stage and at the later grievance/complaint stage.

Overall, our research highlights that the turn to new modes of financing through DFIs, including blended finance mechanisms and PPPs, poses serious challenges to project-affected peoples' access to remedies. Many bilateral DFIs do not have centralised grievance or dispute resolution mechanisms

[6] OECD (2018), 'Making Blended Finance Work for the Sustainable Development Goals', OECD, 29 January 2018.
[7] Bread for the World (2016), 'The Weakest Should Not Bear the Risk', September 2016.
[8] Vervynckt, M (2018), 'An Assessment of Transparency and Accountability Mechanisms at the European Investment Bank and the International Finance Corporation', Eurodad, September 2015).

but rely on fragmented project-level mechanisms which tend to have limited operational independence from their project sponsor and lack independent verification or scope for appeal.[9]

Consequently, there is need for to ensure that DFIs' financing actions and decisions are subject to external accountability mechanisms to allow project-affected peoples to enforce their rights as and when necessary and to obtain an effective remedy in cases where their rights have been infringed.

The Working Group should propose that DFIs' home states develop legislation and regulatory policies to mandate the conduct of human rights due diligence and human impacts assessment in all DFI-financed development projects in line with international human rights standards and environmental law obligations. This domestic legislation and regulation should include provision for access to remedy for project-affected populations beyond corporate due diligence frameworks and project-level grievance mechanisms. Appropriate provision under public administrative law enabling affected populations to seek redress within domestic legal systems, for example, under public administrative law, is necessary given the significant amount of public resources increasingly being directed by governments to DFIs, including financial resources which can be classified as ODA.[10] Therefore, we urge the Working Group to advise DFIs and their home states on establishing independent public oversight of DFI's internal accountability /grievance mechanisms to ensure effective accountability to individuals and local communities.

[9] Tan, 2019, note 1 above.
[10] Saldinger, A (2022), 'Devex Invested: The Rise and Rise of DFIs', Devex.com, 22 November 2022.