Feature

KEY POINTS

- EU and UK reform proposals may become lodestars for other jurisdictions to ensure compliance with United Nations principles.
- In both jurisdictions, policy makers are moving towards transforming best practices and voluntary guidelines into hard legal obligations. Legislative proposals aim to provide legal certainty regarding the human rights obligations that companies face and encourage them to take steps to guard against abuses in their supply chain.
- "Human rights" is a broad concept which is linked to environmental and wider sustainability issues.
- Businesses already face increasing business risk from supply chain issues.

Authors Ferdisha Snagg and Clara Cibrario Assereto

Human rights supply chain due diligence: new legislation on the horizon in the EU and UK

In this article the authors consider recent legislative proposals both in the EU and UK for mandatory corporate environmental and human rights due diligence. They identify key and broader considerations for businesses with respect to supply chain risk management.

In its post-legislative scrutiny report on the UK Bribery Act 2010 (Bribery Act), the House of Lords Select Committee on the Bribery Act reminded us that "[c]ompanies are creatures of statute. They are not corrupt, they do not have consciences, they do not show remorse. But they, and their shareholders, can benefit hugely from the corrupt conduct of their agents, their employees and their directors, sometimes at the highest levels".[1] This is equally true of human rights harms, and creates an imperative to ensure that companies are accountable for adverse human rights and environmental impacts of their own operations and of third-party business relationships. Like with anti-corruption, defining the appropriate policy response to capture varying and increasingly multijurisdictional and complex business models is challenging. However, as business sustainability continues to gain in prominence and urgency, policy makers in the EU and UK are taking steps towards more comprehensive and coherent regulatory frameworks.

INTRODUCTION

On 16 June 2011 the United Nations Human Rights Council endorsed the UN Guiding Principles on Business and Human Rights (UNGPs).[2] The UNGPs are organised around three pillars:

- the State's duty to protect human rights;
- the corporate responsibility to respect human rights; and
- access to remedy for victims of business-related human rights abuses.

They prescribe that in order to meet their responsibility to respect human rights, business enterprises should carry out human rights due diligence to "identify, prevent, mitigate and account for" actual or potential adverse human rights impacts a company may be involved in through its own activities or business relationships. States should adopt a "smart mix" of legislative and other regulatory measures to enforce these obligations and provide redress.

The UNGPs have been widely influential. They have been incorporated into the OECD Guidelines for Multinational Enterprises,[3] and multiple other international standards. The EU and EU member states, and the UK, in particular, have affirmed their commitment to uphold the UNGPs through numerous policy measures, including national laws or legislative proposals. However, calls for mandatory due diligence legislation at the EU level have been growing louder. The UK government has also attracted criticism over the UK's current regulation in this area and been challenged to tackle weaknesses in the framework. Policy makers in both jurisdictions are now moving towards transforming best practices based on the UNGPs into hard legal obligations.

This article aims to provide an overview of the changes that are on the horizon and to identify key, broader, considerations for businesses with respect to supply chain risk management.

THE EU IS WEIGHING ITS OPTIONS FOR EU LEVEL INTERVENTION

On 24 February 2020, the European Commission published a final report on its *Study on due diligence requirements through the supply chain*.[4] The Commission's study was led by the British Institute of International and Comparative Law (BIICL) in collaboration with Civic Consulting and LSE Consulting.

The report heralds important changes in the regulation of corporate supply chain due diligence requirements for identifying, preventing, mitigating and accounting for human rights abuses, in the EU. It observes that existing requirements have not "provided uniformity": a patchwork of standards apply across member states to different sectors and issues. The report's policy analysis is followed by the definition of four alternative EU-level regulatory options:

- Option 1: no change;
- Option 2: new voluntary guidelines;
- Option 3: new corporate reporting requirements; and
- Option 4: mandatory supply chain due diligence as a new legal standard of care.

In line with the title of the study, Option 4 attracts the focus of the report. It is sub-divided into further sub-options:

- Sub-option 4.1: new regulation applying to a narrow category of business (limited by sector);

- Sub-option 4.2: new regulation applying horizontally across sectors:
  - Sub-option 4.2(a): applying only to a defined set of large companies;
  - Sub-option 4.2(b): applying to all business, including small and medium-sized enterprises (SMEs); and
  - Sub-option 4.2 (c): general duty applying to all business plus specific additional obligations only applying to large companies; and
- Sub-option 4.3: sub-options 1 and 2 accompanied by a statutory oversight and enforcement mechanism:
  - Sub-option 4.3(a): mechanisms for judicial or non-judicial remedies; and
  - Sub-option 4.3(b): state-based oversight body and sanction for non-compliance.

The report assesses the advantages and disadvantages of each option and sub-option in terms of its economic impacts and impacts on non-economic issues. It does not recommend any one option or sub-option. However, Option 4 – and a version of this option which applies, with appropriate proportionality, to the broadest scope of businesses and is backed by administrative, civil and possibly even criminal law sanctions – emerges as the option that is most likely to enhance legal certainty for businesses and stakeholders and to ensure a level playing field within the EU.

The report's findings have already impacted the EU's legislative programme. Presenting the study and the report to the European Parliament's Responsible Business Conduct Working Group, on 29 April 2020, the European Commissioner for Justice, Didier Reynders, announced plans by the Commission to introduce rules for mandatory corporate environmental and human rights due diligence in 2021 as part of the European Green Deal.

A CORPORATE DUTY TO PREVENT HUMAN RIGHTS ABUSES MODELLED ON ANTI-CORRUPTION LAW HAS BEEN MOOTED IN THE UK

Any EU laws adopted as a result of the Commission's study and report would not automatically apply in the UK (subject to the terms of any free trade agreement finalised between the UK and EU). However, Brexit does not diminish the relevance of this issue in the UK.

The UK was the first state to implement the UNGPs by publishing a National Action Plan, the implementation of which has resulted, notably, in the introduction of the Modern Slavery Act 2015 (MSA). The MSA requires commercial organisations with a global turnover above £36m to publish an annual slavery and human trafficking statement disclosing any steps the organisation has taken to ensure that human trafficking is not taking place in any of its supply chains or its business. However, a criticism of the MSA is that it can lead to companies taking a tick-the-box approach.

Many have called for more and stronger measures on human rights and business supply chains. On 11 February 2020, BIICL published a report, *A UK Failure to Prevent Mechanism for Corporate Human Rights Harms*.[5] The report examines the legal feasibility of introducing into UK law a corporate duty to prevent human rights harms and produces a model legal clause. The report was based on a UK Joint Committee on Human Rights recommendation to introduce a new legal duty on all companies, including parent companies, to prevent human rights abuses, with failure to do so becoming an offence, along the lines of s 7 of the Bribery Act (see House of Lords and House of Commons Joint Committee on Human Rights Sixth Report of Session 2016-17, 5 April 2017, *Human Rights and Business 2017: Promoting responsibility and ensuring accountability*[6]).

Under s 7 of the Bribery Act, a relevant commercial organisation (RCO) is guilty of an offence if a person associated with the RCO bribes another person, intending to obtain or retain business or a business advantage for the RCO. The offence can be committed in the UK or overseas. The RCO has a defence if it can show, on the balance of probabilities, that it had in place adequate procedures designed to prevent bribery. The Secretary of State must publish guidance about procedures that RCOs can put in place to prevent persons associated with them from bribing as mentioned in s 7 (s 9 of the Bribery Act). Therefore, while there is no substantive requirement for RCOs to have anti-bribery procedures, it is in a company's interest to do so; if it does not have adequate procedures in place, it will have no defence when an associated person bribes another person on behalf of the company. The post-legislative scrutiny of the Bribery Act noted strong praise for the legislation as "an international gold standard for anti-bribery and corruption legislation" – particularly s 7, which has been "remarkably successful". It pointed out that as a result of the legislation "[c]ompanies which might previously have been unconcerned at being involved with bribery (even if [indirectly]) which assisted their business, now have every incentive to put in place procedures to prevent this happening".[7]

Concluding that it would be feasible to model a failure to prevent mechanism for human rights harms on s 7 of the Bribery Act, provided that it is adapted to align with the framework of the UNGPs, the report also sets out a model provision. The key recommendations of the report are:

- A failure to prevent mechanism should apply to all companies, regardless of size or sector, registered, incorporated, formed or carrying on business, or a part of a business, in the UK. Guidance should specify that human rights due diligence procedures may be proportionate to the size of the company, and that SMEs may have more informal processes and management structures than larger companies.
- A failure to prevent mechanism should establish a duty to prevent human rights harms in its own activities and those of its business relationships. The question as to whether a company should be liable for failing to meet this standard of care is to be determined on the facts of each case.
- The legislation must include a defence of procedures "reasonable in all the circumstances", or "reasonable" human rights due diligence, to prevent human rights harms. This should be accompanied by guidance elaborating

on the meaning of "reasonable" due diligence, with reference to the UNGPs, and clarifying that due diligence is accordingly not a "check-box" exercise or a "safe harbour".
- Unlike the Bribery Act, the legislation would only provide for a civil law remedy for damages; however, BIICL expressly stated that this should not be construed as excluding the option of an additional provision for criminal liability.

There is no timeline for legislative consideration of BIICL's proposal and, indeed, no certainty that the proposal will be adopted. Nevertheless, the business accountability for human rights agenda is not likely to go away for UK businesses.

HUMAN RIGHTS AND SUSTAINABILITY ARE LINKED

One of the most striking features of the reform proposals in both the EU and UK is the potentially broad formulation of the scope of rights to be covered by the legislation.

In particular, it is noteworthy that the Commission's study was undertaken under the auspices of the European Commission's March 2018 *Action Plan on Financing Sustainable Growth*[8] and European Parliament resolution of 29 May 2018 on sustainable finance.[9] The expression "sustainable finance" has been defined to refer to the process of incorporating environmental, social and governance (ESG) factors into financial decision-making. For this reason, the Commission's study and report focusses not only on due diligence requirements related to "abuses of human rights, including the rights of the child and fundamental freedoms, serious bodily injury or health risks", but also on "environmental damage, including with respect to climate".

The inclusion of environmental rights (the "E" in ESG) within the scope of rights to be protected by legal due diligence requirements is also present in the UK proposal. The BIICL report recommends that the proposed legislative provision should apply to "human rights" to be defined in a Schedule to the proposed Act and which would include environmental harms. This is because environmental harms "have human rights impacts".

This in our view is indicative of a broader imperative for businesses to ensure that the management of risks related to human rights, the environment and other sustainability matters are operated on a joined-up basis and not on a siloed basis. Businesses will have to operate with a broad mindset of sustainability, responsibility and accountability.

EVEN IN THE ABSENCE OF LEGISLATION, BUSINESSES ARE INCREASINGLY DRIVEN TO INTEGRATE SUPPLY CHAIN DILIGENCE IN THEIR BUSINESS AND RISK MANAGEMENT PROCESSES

The methodology applied by the authors of the EU and UK studies consisted of, largely, survey-based research. The findings indicate that pending finalisation of the respective proposals, EU and UK businesses alike are likely to come under increasing reputational risk, stakeholder activism concerns, litigation risks and other sources of 'peer pressure' to embed best practices on supply chain due diligence.

Based on the EU study:
- 37% c.ca of the companies surveyed stated that they conducted broad-ranging due diligence in relation to the environmental and human rights impacts arising in their operations and supply chains, based on the UNGPs.
- 33% c.ca conducted supply chain due diligence in certain limited areas (such as health and safety, labour, non-discrimination and equality, environmental, land rights and indigenous communities).
- 7% c.ca indicated that they undertook due diligence with respect to the environment and climate change but not with respect to human rights.
- 7% c.ca indicated that they did not undertake any form of due diligence for any human rights or environmental impacts.
- Due diligence practices within SMEs appeared to be slightly less established than in companies with over 1,000 employees.
- The "vast majority" of business respondents expressly included environmental impacts in their due diligence. These typically included the environment, air pollution and greenhouse gas emissions, climate change and biodiversity.
- 55% c.ca indicated that income inequality is expressly included in their due diligence, and c.45% indicated that it is "implied as included (though not expressly mentioned)".
- 26% c.ca included profit-shifting to lower tax jurisdictions in their due diligence, but for c.74% it is "implied as included".
- The actions which companies most frequently take to prevent, mitigate or remedy the adverse human rights and environmental impacts of their operations include clauses in supplier contracts, codes of conduct, audits, training, working with human rights and environmental experts and additional dedicated staff for human rights or environmental measures.
- Most businesses diligence first tier suppliers only, but some go further up the supply chain.
- In general, questions as to how to link wider social impacts with a company's own individual impacts and due diligence efforts are still relatively new.
- The business representatives surveyed put reputational risks and demands by investors and consumers as the most relevant drivers for undertaking supply chain due diligence. Investors requiring a high standard and consumers requiring a high standard followed. Legal requirements appeared as the least important motivation.

Regulation in this area was largely perceived as beneficial. Respondents to the surveys felt that the current legal landscape does not provide companies with an efficient and coherent framework, and legal certainty, with respect to their human rights and environmental due diligence obligations. The benefits of a mandatory supply due diligence standard were thought to include:

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Ferdisha Snagg and Clara Cibrario Assereto are associates at Cleary Gottlieb Steen & Hamilton LLP. They specialise in EU and UK financial services regulation.
Email: fsnagg@cgsh.com and ccibrarioassereto@cgsh.com

- legal certainty (and in the EU, harmonisation);
- increased competitiveness;
- increasing leverage in business relationships throughout the supply chain through a non-negotiable standard; and
- providing injured parties with effective redress.

Some interviewees in the EU study indicated that an EU-level regulation would be a powerful incentive insofar as it could be linked to legal requirements for operating in or accessing the European market. Indeed, the EU has made safeguarding of human rights and fundamental freedoms, as well as so-called "level playing field" matters – including in relation to social and employment standards, the environment and climate change – key requirements of the proposed free trade agreement with the UK. This approach would likely lead to a convergence of EU and UK standards as well as the internationalisation of those standards. Regardless, business and human rights is likely to remain a priority for regulators and businesses' stakeholders. Businesses must engage with human rights, environmental issues and ESG, more broadly, keeping in mind that diligence failures carry increasing risk. ■

1 See https://publications.parliament.uk/pa/ld201719/ldselect/ldbribact/303/303.pdf, para 167.
2 UN Office of the High Commissioner for Human Rights *Guiding Principles on Business and Human Rights: Implementing the 'Protect, Respect and Remedy' Framework*, HR/PUB/11/04, 2011.
3 Available at: https://www.oecd.org/daf/inv/mne/48004323.pdf.
4 The report is available at: https://op.europa.eu/en/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75ed71a1/language-en.
5 Available at: https://www.biicl.org/documents/84_failure_to_prevent_final_10_feb.pdf.
6 Available at: https://publications.parliament.uk/pa/jt201617/jtselect/jtrights/443/443.pdf.
7 See para 176.
8 Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52018DC0097.
9 Available at: https://www.europarl.europa.eu/doceo/document/TA-8-2018-0215_EN.html.

Further Reading:

- Social impact investing: market trends and risks (2020) 1 JIBFL 61.
- The emerging human rights liability of banks? (2016) 6 JIBFL 353.
- LexisPSL: Overviews: Responsible business and human rights – overview.