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Doubling down: time for a bold framework for human rights due diligence

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1. Introduction

The European and Council proposal Directive on Corporate Sustainability Due Diligence ('CSDDD') proposes bold reforms with the potential to change business practices of all EU and non-EU corporations. CSDDD is a welcomed voice calling for a new covenant between corporations and society where corporations must respect international human rights and environmental law as being core to their business. This Article provides a focused look on the extent of the corporation's human rights due diligence obligations under CSDDD vis a vis its business partners operating along its value chain, and then turning its attention to financial services. Although I focus on human rights, much of what is said will also be relevant to environmental due diligence.

I challenge two key features of the CSDDD proposal, which must be resolved during the trilogue rounds between the EU institutions. The first challenge relates to the scope of the corporation's human rights due diligence across the value chain and the obligations which arise vis a vis its business partners and beyond. I show that the obligation to conduct human rights due diligence should not be limited to identifying and removing adverse impacts directly caused by the corporation or its subsidiary. Instead, I advocate that the initial proposal by the Commission to include all adverse impacts along the entire value chain should be restored, and strengthened by adopting contractual ethics based on cooperatism, openness, and good faith.

The second challenge relates to the inexplicable desire by all three EU institutions to exempt financial institutions from the obligations under the CSDDD either partially or by creating a special carveout for financial services. Both options undermine the applicability of internationally recognised human rights to all corporations regardless of their size or sector. It is also indefensible to exempt actors with substantial impact on society and environment, and also a sector which is well versed, though as will be seen imperfectly, in conducting human rights due diligence under the Equator Principles ('EPs').

2. Background

The European and Council proposal Directive on Corporate Sustainability Due Diligence ('CSDDD'), which is currently undergoing interinstitutional negotiations between the European Parliament ('EP') and the Council of the European Union ('Council') includes bold reforms which if adopted will change business practices of all EU and non-EU corporations which are covered under its scope¹. Although it is certain from the current

¹ The most recent draft was proposed by the European Parliament (first reading) on the 1 June 2023. P9_TA(2023)0209 Corporate Sustainability Due Diligence Amendments adopted by the European

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drafts that much more needs to be done to make corporations stand in line and comply with the rich body of international human rights law, and that there are clear gaps in terms of its scope, theory and practical challenges which are hard to avoid, this should not distract of the importance of the CSDDD for the advancement of fundamental values that the UN has unanimously agreed in the United Nations Guiding Principles on Business and Human Rights² ('UNGPs').

In the past decade or so, much effort has gone into operationalising of the UNGPs with sector specific models or toolkits advising corporations on how to conduct human rights due diligence, the extent of their duties, and designing or engaging remediation process of business related human rights violations. The financial industry is one such industry³. One should not lose sight that the UNGPs have introduced a soft normative framework, and although they made it clear that the source of the corporation's responsibility to respect human rights is jurisprudentially based in international human rights law, and international labour law⁴, it stopped short of imposing binding obligations on corporations. In other words, except under few specific domestic⁵, or regional rules that

Parliament on 1 June 2023 on the proposal for a directive of the European Parliament and of the Council on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937 (COM(2022)0071 – C9-0050/2022 – 2022/0051(COD)). Available https://www.europarl.europa.eu/doceo/document/TA-9-2023-0209_EN.pdf. See also the Council draft Proposal for a Directive Of The European Parliament And Of The Council on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937, 30 November 2022 available <https://data.consilium.europa.eu/doc/document/ST-15024-2022-REV-1/en/pdf>. See also Commission draft-Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937, COM (2022) 71, 2022/0051 (COD), 23 February 2022 available https://eur-lex.europa.eu/resource.html?uri=cellar:bc4dcea4-9584-11ec-b4e4-01aa75ed71a1.0001.02/DOC_1&format=PDF. There are various formulations in the various drafts of the CSDDD which have been put forward by the Commission, Council of the European Union and the European Parliament. Much will depending on the corporation size, revenue, their sector or a combination of any of these factors

² Office of the High Commissioner for Human Rights, 'Guiding Principles for Business and Human Rights: Implementing the United Nations "Protect, Respect and Remedy" Framework' UN New York and Geneva 2011, HR/PUB/11/04, https://www.ohchr.org/sites/default/files/documents/publications/guidingprinciplesbusinesshr_en.pdf

³ OHCHR Response to Request from BankTrack for Advice Regarding the Application of the UN Guiding Principles on Business and Human Rights in the Context of the Banking Sector. 12 June 2017 available at <https://www.ohchr.org/sites/default/files/Documents/Issues/Business/InterpretationGuidingPrinciples.pdf>. See Equator Principles EP4 July 2020 which set a private industry initiative available at <https://equator-principles.com/app/uploads/The-Equator-Principles-EP4-July2020.pdf>. See specific OECD Due Diligence Guidance for Responsible Business Conduct (2018) and OECD sectoral guidance, available at: <https://mneguidelines.oecd.org/mneguidelines/>.

⁴ Principles 12 of the UNGPs, (n 2)

⁵ In the UK Modern Slavery Act 2015 < <https://www.legislation.gov.uk/ukpga/2015/30/contents/enacted>>. In France see the French Commercial Code (French Duty of Vigilance Law) In Germany see the Act on Corporate Due Diligence Obligations in Supply Chains of 16 July 2021 <https://www.csr-in-deutschland.de/SharedDocs/Downloads/EN/act-corporate-due-diligence-obligations-supply-chains.pdf?blob=publicationFile>.

impose human rights obligations on corporations⁶, international human rights law does not directly apply to corporations⁷.

This lack of a binding framework has allowed some corporations to turn an eye on human rights violations done by their subsidiaries⁸, or operations along their value chain carried out by direct or indirect business partners that violate international human rights law. More so, some corporations managed to outsource so to speak their problematic activities to jurisdictions with weak human rights governance driven by an ever need to generate profit at the expense of the right to fundamental human rights. Luckily, the elephant in the room, ie the soft normative framework for corporate accountability to human rights could not remain unshaken, impelling some states and non-governmental organisations to require a binding international framework for business obligation to respect human rights⁹.

Nevertheless, even when considering all the shortcomings of the CSDDD, it should be viewed as welcomed initiative where corporations must respect human rights as being core to their business as opposed to being collateral responsibilities¹⁰, or mere externalities¹¹. Corporations must avoid or remove actual or potential adverse human rights impacts linked to their activities or activities which are linked to them through their direct or indirect business relationships¹².

3. The duty to conduct human rights due diligence in view of preventing, removing, and mitigating adverse impact.

Among the stated objectives of the CSDDD is to resolve the gaps in current voluntary standards on responsible business conduct such as the UNGPs and the OECD guidelines¹³ recognising that such standards have had limited effect due to the complexities of value chains, market pressures, and costs associated with their implementation¹⁴. The CSDDD, however, proposes a framework which differs substantially from the UNGPs in relation to three key matters. First, the CSDDD is limited

⁶ Directive 2014/95/EU amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups (OJ L 330, 15.11.2014, p. 1–9). Regulation (EU) 2017/821 of the European Parliament and of the Council of 17 May 2017 laying down supply chain due diligence obligations for Union importers of tin, tantalum and tungsten, their ores, and gold originating from conflict-affected and high-risk areas (OJ L 130, 19.5.2017, p. 1–20).

⁷ the UNGPs has not resolved the subjectivity problem of corporation to international human rights law. See Andrew Clapham, *Human Rights Obligations of Non-State Actors*, 2006 Oxford University Press, chapter 2 and 3.

⁸ *Jesper v Arab Bank*, 584 U.S. (2018), 13; *Kiobel v. Royal Dutch Petroleum Co.*, 569 U. S. 108, 621 F.3d, 118.

⁹ <https://www.business-humanrights.org/en/big-issues/binding-treaty/>

¹⁰ Sheldon Leader, 'Collateralism', in Roger Brownsword (ed.) *Global Governance and the Search for Justice*, Oxford: Hart Publishing (2005).

¹¹ Alessio M. Paccès, 'Civil Liability in the EU Corporate Sustainability Due Diligence Directive Proposal', at <https://blogs.law.ox.ac.uk/oblb/blog-post/2023/09/civil-liability-eu-corporate-sustainability-due-diligence-directive-proposal>

¹² Principle 13 of the UNGPs (n 2). See recital 5 of the CSDDD Parliament draft (n 1). See Recital 13 of Council CSDDD draft (n 1).

¹³ OECD Guidelines for Multinational Enterprises (2011 update), available at: <https://doi.org/10.1787/9789264115415-en>, with set of recommendations on responsible business conduct.

¹⁴ Commission draft, explanatory memorandum, part 1, (n 1).

in its scope. It does not apply to all corporations. Article 1 of all drafts includes various formulations which limits the application of the Directive to primarily large corporations¹⁵. Second, as will be shown below the CSDDD does not apply to all sectors. Third, the CSDDD does not expressly state that corporations covered under its scope are bound by all internationally recognised human rights law, unlike the comprehensive and universal approach to human rights under the UNGPs¹⁶. Instead, it includes a list of those international law provisions that the corporations must respect in Annex I, which do not cover some important rights such as those relating to free movement of migrant workers¹⁷.

The CSDDD imposes concrete obligations on corporations covered under its scope to conduct human rights across its value chain, in relation to their operations, members of its corporate group, or entities with whom the company has an established business relationship, in order to prevent or remove human rights violations or mitigate any adverse impact they may have¹⁸. It also imposes a statutory liability regime under Article 22 of the Directive¹⁹. Corporations must prioritise the prevention of human rights violations over their mitigation or remediation, which is a recurring theme in all international soft and hard normative frameworks.

One important feature of the UNGPs is that they recognise that there is no ideal solution and that in practice, human rights risks vary by industries and contexts. 'Companies are not being asked to guarantee in all circumstances that adverse impacts will be either prevented or removed', which also means that the nature of the duty to conduct due diligence is risk-based, a point which was endorsed by the EP and Council drafts of the CSDDD²⁰. Any risk which is highlighted as part of the due diligence identification exercise must be assessed 'based on severity and likelihood of the adverse impact'.²¹ High risk situations require a more extensive due diligence. Moreover, where it is not possible to address all identified impacts at the same time, a corporation should address the impact beginning with the one deemed to represent the highest risk in accordance with its severity and likelihood, and then following the removal or mitigation of that threat

¹⁵ This may amount to various stopcocks which prevent its binding nature to trickle down to smaller corporations.

¹⁶ UNGPs state that corporations have the responsibility to respect all human rights including the International Bill of Human Rights (that is, the Universal Declaration of Human Rights, the International Covenant on Civil and Political Rights, and the International Covenant on Economic, Social and Cultural Rights), core international labour Organisation Conventions as well as to UN instruments which have elaborated on the rights of specific groups or populations such as women, children, Indigenous peoples, and migrant workers. The OECD guidelines also specify that in situations of armed conflict, enterprises should respect the standards of international humanitarian law. see Amnesty International, *Closing the Loopholes Recommendations For An Eu Corporate Sustainability Law Which Works For Rightsholders*, 50. OECD, OECD Guidelines for Multinational Enterprises, 2011, p32, <http://mneguidelines.oecd.org/guidelines/> 51.

¹⁷ Amnesty report page 17
<file:///ueahome/eresssf1/fpb16tdu/data/Downloads/IOR6065392023ENGLISH.pdf>

¹⁸ CSDDD (n 1)

¹⁹ Article 22 of the CSDDD (n 1)

²⁰ EP CSDDD draft (n 1). See also Article 4(1) of the EP draft which states 'Member States shall ensure that companies conduct risk-based human rights and environmental due diligence'.

²¹ OECD, Due Diligence Guidelines for Responsible Business Conduct, 2018, p23, <http://mneguidelines.oecd.org/OECD-Due-DiligenceGuidance-for-Responsible-Business-Conduct.pdf>

corporations should proceed to the 'less significant impacts'.²² This risk-based approach holds the key to resolving the challenges I address in this Article, namely that human rights due diligence should apply to the entirety of the value chain, and that the Council or EP should not make specific concessions or enable carveouts to the financial sector, a point which I will return to in the next parts of this Article.

The next section analyses Articles 5 to 8 of the CSDDD which impose, *inter alia*, core obligations on corporations to oversee that its value chain is free from actual and potential human rights violations in relation to corporate activities with business partners with whom the corporation has an established business practice (entities). The CSDDD requires corporations to leverage their contractual relationships with their business in order 'to affect change in the practices of the entity causing or contributing to the adverse impact'²³. This is meant to be done through a practice of cascading of terms which essentially give effect to corporation's code of conduct containing its human rights due diligence policy, and by that force entities along the entire value chain to commit to the minimum international human rights law included under Annex I of the CSDDD.

4. Business partners and contractual Cascading

UNGPs state that corporations have the responsibility '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'²⁴. Article 5 of the Council draft of the CSDDD stipulates that corporations should put in place governance, a due diligence policy which among other things contain a code of conduct describing rules and principles to be followed by the company's employees, subsidiaries and the company's direct or indirect business partners²⁵.

The EP draft omits any reference in Article 5 to direct or indirect business partners and instead requires of the corporation to include a code of conduct which defines 'rules and principles and measures to be followed and implemented where relevant throughout the company and its subsidiaries across all operations'²⁶. This omission although seemingly minor it may nonetheless create incoherency in terms of the type of obligations which can be cascaded to all actors that affect the value chain of the corporation and may indeed therefore stand in the way of developing wider industry standards that could assist in positively influencing the widest range of economic activities along the value chain however remote these activities might be.

In relation to adverse actual or potential impact arising out of the activities of their business partners, corporation must seek contractual assurances from those entities that will ensure compliance with the corporation's code of conduct and, as necessary, a prevention action plan, including by seeking corresponding contractual assurances from its partners to the extent that their activities are part of the company's chain of activities. Corporations should provide targeted and proportionate support for an SMEs with which

²² Overview of Due Diligence for Responsible Business Conduct, <https://mneguidelines.oecd.org/OECD-Due-Diligence-Guidance-for-Responsible-Business-Conduct.pdf>, p 17.

²³ Article 3 (1) (q) Parliament draft (n 1).

²⁴ UNGPs (n 2), principle 13.

²⁵ Article 5(1a)(b) of the CSDDD Council draft (n 1)

²⁶ Article 5(1(b) of CSDDD EP draft (n 1)

they have an established business relationship and collaborate with other entities, including, where relevant, to increase the company's ability to bring the adverse impact to an end'²⁷.

Corporations are required to prevent, remove or mitigate the adverse impacts by for example make necessary financial or non-financial investments, "or offer low interest loans to the entity, or guidance such as training or upgrading management systems". The overall impression is that corporations should also adapt business models, change business practices such as purchase practices, and find ways to support their business partners to prevent the adverse risk including to ways to contribute to 'living wages and incomes for their suppliers'.²⁸

The above requirements operate within contractual relationships that may have been accustomed to a more individualist model in the sense that parties look for the maximisation of their economic benefit even if at the expense of the other contractual party. The CSDDD appears to challenge this culture, an issue which I will address in the next part.

5. Termination as a last resort, and the duty of cooperative ethics

Often human rights violations along the value chain occur because of a disconnect between the buyer's objective to obtain goods and services at the lowest price possible, and the need to safeguard human rights which belongs to all stakeholders whether privy to the contract or otherwise. There is an inevitable trade-off between both objectives. Therefore, at the heart of the problem is the individualist ethics which has dominated contractual practices for far too long²⁹. The CSDDD is set to challenge the individualist ethics. Where human rights due diligence is involved, contractual parties must have some level of regard, even a robust one, to the economic interest of the other party³⁰. Buyers therefore cannot hide behind contractual terms and terminate the contract at free will because a business partner had breached its code of conduct, when there were measures which are less extreme which can be followed and which will help the prevention, removal or mitigation of the human rights adverse risk from the value chain. This signals a much welcomed and more effective endorsement of cooperative ethics.

Thus, though perhaps unintended, the CSDDD changes the fundamentals of individualist ethics often experienced in aggressive free market economics supported by contractual doctrines where contractual remedies for breach of contract are party centred and where the law forgives a party which seeks to maximise its profit or avoid a contract because they can, even if it creates harsh conditions, including human rights adverse risk to the other party or to a legitimate third party stakeholder. For example, a breach of a term classified as a condition by the contractual parties entitles the innocent party to terminate the contract and seek damages irrespective of the seriousness of the breach or the impact it has on the innocent party³¹.

²⁷ Recital 38 of the EP Draft

²⁸ 7(2)(ca) of CSDDD EP draft (n 1).

²⁹ Roger Brownsword, 'Individualism, Cooperativism and an Ethic for European Contract Law', 63 *MLR* (2001) 628, 630-631

³⁰ *Ibidem*.

³¹ *Lombard North Central Plc v Butterworth* [1989] QB 527.

The CSDDD is set to change this approach where human rights are at stake. In such situations corporations must adopt cooperative ethics by supporting each other, refrain from the termination of business relationship in view of allowing business partners to remove or mitigate the human rights adverse impacts through a 'targeted and proportionate support to the SMEs' with whom they have business relationships³². It is recognised that unilateral termination may in fact exacerbate the human rights violations or lead to a more severe human right impact, such as in the case where the intention is to remove child labourers from the value chain the termination of the contract may condemn the child labourers to even more severe conditions³³. Be it as it may, provided some conditions are met, all drafts of the Directive allow a corporation to terminate the contractual relationship with business partners as a last resort when no less drastic possibilities are available³⁴.

This is a welcomed development by the CSDDD however it must be reinforced by including an express general obligation in the CSDDD to conduct due diligence in good faith, and when a human rights risk is identified (also potentially), parties must engage in accordance with cooperative ethics in view of removing or mitigating the adverse impact. This is important and will have a meaningful and real results because 'Good faith goes to the heart of the contract' and helps to determine how parties should relate to each other³⁵. Moreover, this duty will not be viewed by Member States as burdensome because most Member States do recognise a general duty to observe principles of fairness and good faith under their contract law traditions³⁶. The observance of general principles of fairness, openness, and cooperative ethics should in the long run lead to industry solutions to the type of problems often experienced on the industry-specific value chain. The CSDDD does however allow a corporation not to terminate the relationship with a crucial business partner even where it was not possible to remove the adverse impact where termination will cause the corporation substantial financial such 'as an effect giving rise to the likelihood of insolvency', or legal prejudice resulting from the fact that the business partner provides 'raw material, product or service essential to the company's business'³⁷.

6. Financial services.

The UNGPs apply to all business enterprises, including commercial banks and other entities in the financial sector, regardless of 'size, sector, operational context, ownership and structure'³⁸. The UN Working Group on Business and Human Rights recognized that 'financial actors have an unparalleled ability to influence companies and scale up on the

³² Recital 38 of the CSDDD EP draft (n 1).

³³ Recital 36 of the CSDDD EP draft (n 1).

³⁴ Articles 7 and 8, and recital 36 of EP Draft (n 1).

³⁵ Brownsword, R. (n 29) p 630.

³⁶ *Ibid*, p 628.

³⁷ Recital 36 of CSDDD EP draft (n 1). See also Articles 7 and 8 of the CSDDD.

³⁸

<https://www.ohchr.org/sites/default/files/Documents/Issues/Business/InterpretationGuidingPrinciples.pdf>, p 3. This is also the approach under the Organisation for Economic Co-operation and Development (OECD) Guidelines for Multinational Enterprises on Responsible Business Conduct.

implementation of the Guiding Principles'³⁹. In the Equator Principles, which include the relevant provisions of the Guiding Principles, the signatories from the financial sector state that they 'recognise that our role as financiers affords us opportunities to promote responsible environmental stewardship and socially responsible development, including fulfilling our responsibility to respect human rights by undertaking due diligence in accordance with the Equator Principles'⁴⁰.

All three drafts of the CSDDD by the European Commission, Council, and EP include reduced obligations of due diligence for the financial sector. For example, the Commission's proposal requires of financial institutions to only conduct due diligence in relation to 'their direct clients (and other companies in the same direct group should they exist) and only before providing the loan or other service but not in an ongoing manner'. Moreover, financial institutions do not have to conduct due diligence in relation to small and medium sized enterprises even when they are a direct client. The Council draft created a carve out for the financial sector, leaving it to individual member states to decide whether to include it once the directive is transposed into national law.⁴¹

Similarly, the EP draft includes a limited version of human rights due diligence obligation. Article 6(3) stipulates that 'when corporations covered under the scope of the CSDDD provide financial services, identification of actual and potential adverse human rights impacts and adverse environmental impacts shall be carried out before providing that service and before subsequent financial operations, and, if notified of possible risks by means of the procedures referred to in Article 9, during the provision of the service'⁴². This is an improvement on the commission's proposal which only requires of corporations to conduct the human rights due diligence only up to the time before the provision of the financial service⁴³, which is also a much-improved position than that included in the Council's draft which has introduced a carveout for financial services from the scope of the CSDDD⁴⁴.

As stated above these three variant positions of the EU's institutions flies in the face of the text and the spirit of the UNGPs. I have also highlighted above that the nature of the human rights due diligence is risk-based. Accordingly, even complex financing processes which may depend on 'the size of the bank, the nature and context of its operations and the severity of the bank's potential adverse human rights impacts', may be addressed by following a risk-based approach which relies on the severity and likelihood of the adverse impact when determining 'the complexity of the due diligence service'.⁴⁵ Financial institutions can therefore prioritise their human rights due diligence processes and how they respond to adverse impacts in accordance to the risk-based approach.

³⁹ Financial Sector and the and the European Union Corporate Sustainability Due Diligence Directive, <https://www.ohchr.org/sites/default/files/documents/issues/business/workinggroupbusiness/Statement-Financial-Sector-WG-business-12July2023.pdf>

⁴⁰ Ibid.

⁴¹

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⁴² See Article 6(3) of the EP draft (n 1).

⁴³ Ibid.

⁴⁴ A. M. Paccès, (n. 11).

⁴⁵ OHCHR, The Corporate Responsibility to Respect Human Rights: An Interpretive Guide, p. 19 (2012).

In practice, most financial products will create a direct 'direct linkage' between the bank and the business partner. The UNGPs envisage causality between the human rights adverse impact and the financial product, for example where a client of the bank uses the financial service or product in a way that causes (or potentially risks) human rights adverse impacts.⁴⁶

To conclude, there isn't a policy or practical reason why financial institutions should be exempt or be partially relieved from the obligations arising under the CSDDD. In fact, as will be seen under part 3.3 of this Article, financial institutions are best placed to make a quick transition into the new framework because of the valuable experience gained from the operationalisation of the UNGPs to the financial sector under the Eps. Whilst as will be seen the Eps are imperfect, they can nonetheless be improved by the binding framework proposed by the CSDDD.

7. The Equator Principles (Eps')

EPs is an industry initiative adopted by Equator Principles Financial Institutions (EPFIs)⁴⁷, are a voluntary set of principles, which ensures that social and environmental issues are observed when EPFIs provide loans or debt finance for infrastructure projects⁴⁸. Their primary mandate is to assess, monitor and report environmental and social risk in project finance, project finance-related corporate loan investments, and bridge loans⁴⁹. They require of adhering financial institutions to impose a condition on borrowers when agreeing to finance a project to abide by the EPs and establish a grievance mechanism for the resolution of disputes concerning their social and environmental impact.

EPs recognise that EPFIs who provide the debt finance to make project deals happen, are in a strong position to negotiate and influence the terms of the contractual agreements regarding to social and environmental factors⁵⁰. All EPFIs have undertaken not to provide loans if any of the project sponsors refuses to comply with the EPs, or are unable, to prove that the project will be constructed and operated in accordance with the environmental, social and governance considerations stated in the EPs⁵¹.

⁴⁶

<https://www.ohchr.org/sites/default/files/Documents/Issues/Business/InterpretationGuidingPrinciples.pdf>, 6

⁴⁷ Certain banks and other financial institutions who signed up to the EPs. See Patrick Bell, *The Equator Principles Explained*, Lexology, February 16 2012.

<https://www.lexology.com/library/detail.aspx?g=418bbbd0-514b-4277-950e-c2585ab67fc4>.

⁴⁸ *Ibid.*

⁴⁹ Equator Principles Reporting Criteria, Green Investment Group, August 2017.

http://www.greeninvestmentgroup.com/media/180098/gib-equator-principles-817_01.pdf, accessed on 23 November 2023

⁵⁰ P. Bell (n 47).

⁵¹ P. Bell (n 47).

Principle 6 EPs⁵², which is designed to help manage the social and environmental risks associated with international project finance⁵³, requires the client in certain type of projects to ‘establish a grievance mechanism designed to receive and facilitate resolution of concerns and grievances about the Project’s environmental and social performance’. It stipulates that such grievance mechanisms should be transparent, culturally sensitive, and efficient by resolving grievances promptly and free of charge to use. Such mechanisms must coexist with other means of access to justice and should not deny the aggrieved party access to judicial or administrative remedies⁵⁴.

The main weakness of the EPs is that they do not provide robust institutional support to the implementation of the principles, including the overseeing of the proper administration of the grievance mechanism envisaged under principle 6. They do not provide standards for review body, formal transparency, or implementation requirements or mandated compliance procedures. The most they do is to impose weak reporting requirements to the EPFI under principles 7 and 8. One serious shortcoming is that such grievance mechanisms do not operate between victims and the EPFIs (lending institutions) themselves⁵⁵, and lack enforcement power necessary to police the financial institutions involved in the project finance⁵⁶, which led some to argue that Principle 6 is merely an internal mechanism EPFIs used to limit their own risk exposure⁵⁷.

Moreover, Principle 6 EPs does not establish grievance processes that provide for external accountability⁵⁸. It fails to consider many of the values envisaged under Principle 3 of the EPs, except for the requirements of accessibility and transparency, the latter, unlike the meaning given to it by Principle 31 UNGPs, operate vis a’ vis the victim and corporation to the exclusion of external stakeholders. Moreover, Principle 6 EPs does not include any minimum obligatory due process standards that project sponsors must meet⁵⁹.

Like the UNGPs it does not provide a procedure for affected populations and stakeholders, instead it relegates this responsibility to the corporation. The problem with this is that banks and financial institutions sometimes do not have the ability to monitor and enforce compliance due to the lack of expertise and resources to work effectively with local

⁵² The Equator Principles EP4 July 2020. <https://equator-principles.com/app/uploads/The-Equator-Principles-EP4-July2020.pdf>. It is a risk management framework, adopted by financial institutions.

⁵³ Thomas Papadopoulos, ‘The Greening of Project Finance: Is This a Viable Project?’ 7 *ICFA U.J. of Banking L.* (2009) 8, 9-12.

⁵⁴ The Equator Principles EP4 (n 3).

⁵⁵ David M. Ong, ‘Public Accountability for Private International Financing of Natural Resource Development Projects: The UN Rule of Law Initiative and the Equator Principles’, 85 *Nordic Journal of International Law* (2016) 201, 228. See also Benjamin J. Richardson, ‘Financing Sustainability: The New Transnational Governance of Socially Responsible Investment’, 17 *Yearbook of International Environmental Law* (2008) 73, 92.

⁵⁶ Niamh O’Sullivan & Brendan O’Dwyer, ‘Stakeholder Perspectives on a Financial Sector Legitimation Process: The Case of NGOs and the Equator Principles’, 22 *ACCT. Auditing & Accountability J.* (2009) 553 567-68.

⁵⁷ Joshua A Lance, ‘Equator Principles III: A Hard Look at Soft Law’, 17 *North Carolina Banking Institute* (2013) 175, 182.

⁵⁸ *Ibid*, 176.

⁵⁹ D. M. Ong (n 55) 228.

governments and communities⁶⁰. The upshot of all of this is a grievance mechanism model, which its success relies significantly on the good will of the corporation⁶¹. As claimed above such a model is weak in terms of holding corporations to account, as well as with regards to satisfying the legitimacy requirement and the delivery of rights-based outcomes. Regrettably, there isn't much evidence or data to support the existence of successful grievance mechanisms organized under principle 6 of the EP.

The EP however will strengthen if the CSDDD is also applied to financial institutions. All EP members should meet one of the scope formulations under Article 1 and available in the various drafts. The CSDDD demands a strong monitoring of the observance and implementation of human rights due diligence, and also a robust dispute resolution process which complies with principle 31 of the UNGPs, and which provides direct access to victims of business-related human rights violations wherever the violation happened along the value chain⁶².

8. Conclusions

EU lawmakers are currently negotiating the final text of the CSDDD in trilogue and are expected to reach agreement in early 2024. It has been demonstrated that as a matter of policy the human rights due diligence should apply to the entirety of the value chain. The EU institutions should double down on the need to make corporations respect international human rights and reinforce cooperative ethics in the relationship between corporations and their business partners. This should improve the prospect of successfully preventing, removing or mitigating adverse human rights impacts, and lead to a more sustainable solution among all actors on the value chain, including indirect business partners who do not have contractual relationship with the corporation.

Moreover, EU institutions must stay steadfast in the face of any temptation to depart from long established principle under the UNGPs that human rights apply to all organs of society regardless of size and sector. I have demonstrated that the risk-based approach should in principle alleviate any concern about the application of human rights due diligence processes to complex financial products. It can and should be done.

⁶⁰ Robert F Lawrence, William L Thomas, 'The Equator Principles and Project Finance: Sustainability in Practice', 19 *National Resources & Environment* (2004) 20, 25.

⁶¹ J. A. Lance. (n 57) p 177.

⁶² See Article 9 of the CSDDD (n 1).