DISCUSSION PAPER | May 2019

IRBC Agreements
Dutch Banking Sector Agreement

Discussion paper

Working Group enabling remediation

Supported by SER

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1 Introduction: Purpose and Scope of this Discussion Paper

The Dutch Banking Sector Agreement: The Dutch Banking Sector Agreement (DBA) on International Responsible Business Conduct Regarding Human Rights was signed in October 2016 by the Dutch Banking Association (NVB), Dutch banks, trade unions, NGOs, and the Dutch Government. Through the agreement, adhering banks made individual commitments towards meeting their individual responsibility to respect human rights under the OECD Guidelines and the UNGPs, and the NVB and civil society and government counterparts committed to supporting adhering banks in those efforts. The agreement focused on two areas of banking activity, corporate lending and project finance. [1]

The Working Group on Enabling Remediation: Under the agreement, the parties established several multi-stakeholder working groups to further explore and support implementation of specific areas of the agreement, including a Working Group on Enabling Remediation. This discussion paper summarizes the most important points of conversation, consensus and broadly shared insights from this Working Group, while recognizing within the paper where perspectives among the group diverge and consensus was not reached. It provides a menu of options for action that banks could take to enable remediation, without being prescriptive. They should not be read as steps every bank must take to meet their responsibility. Both the UNGPs and the OECD Guidelines allow for substantial flexibility in how institutions might seek to meet the expectations outlined in the guidelines. The WG recognizes that many of the ideas are still exploratory, and hopes that this paper can catalyse further discussion to develop practical tools and approaches.

- **Purpose:** The purpose of the Working Group was to explore the responsibility of banks for enabling remedy for impacts they might be connected to through their client relationships, and to explore the roles that banks could play in meeting this responsibility more effectively in practice.[2] The intent of the Working Group was to generate insights and learnings that would be relevant not only for Dutch banks, but for the broader global community.

1 The parties agreed to delay a focus on asset management activities, in order to allow collaboration and alignment with other financial institutions and institutional investors. These conversations are now underway.
2 Paragraph 7.4 of the Dutch Banking Sector Agreement on international responsible business conduct regarding human rights

- **Why the conversation is important:** The Working Group's conversations have two broad intended outcomes, both of which are aimed at improving outcomes for people who might be harmed by business activities connected to the corporate lending and project finance activities of banks:
  - First, *to ensure that remedy is available to affected stakeholders when negative impacts occur*. Members of the Working Group recognize that globally, there are impacts resulting from business activities for which remedy is not currently available in practice, and that banks may be connected to these impacts through their client relationships and their clients' extended value chains.
  - Second, by creating greater alignment on understanding of the responsibility for remedy, *to promote adequate and effective human rights due diligence practices by banks in order to assess, prevent and mitigate impacts before they occur*.

Participants: The Working Group included representatives from the parties to the agreement, a number of the adhering Dutch banks and several external experts identified by the members of the Working Group (members of the Working Group are listed in Annex 2). The NVB had a facilitating role for the representatives of the participating banks in this Working Group.

Questions Addressed by the Working Group: The Working Group sought to align understanding among parties on **two broad areas**, in situations where a bank might be connected to harm to people through the activities of a client. These can be summarized as follows:

Question 1: How is a bank deemed connected to adverse human rights impacts in connection to their corporate lending and project finance activities? Under the OECD Guidelines and the UNGPs, this requires analyzing under what circumstances a bank might 'cause' an impact, 'contribute' to an impact, or have its operations, products or services 'linked' to an impact through a business relationship. This analysis then determines the nature of the bank's responsibility for action, including whether the bank should provide or contribute to remedy for the harm that occurred or use its leverage to enable remedy is provided by other parties.

Question 2: What types of actions could a bank take, and what appropriate roles could a bank play, to enable remedy more effectively in practice, recognizing that the specific responsibility of a bank with regard to remedy will depend on how the bank is connected to the impact?

Meetings of Working Group: The Working Group held meetings together over the course of 2017 and early 2018, focused primarily on Question 1 above, including joint case-based analysis, literature review, expert inputs, and additional preparation and inputs between meetings. Additional meetings in 2018 and early 2019 focused on Question 2 above.

Working Group conversations sought to explore the circumstances under which a bank might have a responsibility to contribute to remedy for a specific impact, because it contributed to the harm, rather than solely using its leverage with other parties to address an impact, because it was directly linked to the impact. We recognized that the adequacy of a bank's due diligence process played an important role in determining whether the bank might have facilitated an impact through an omission – a failure to take appropriate steps in the due diligence process. We therefore sought to explore what adequate due diligence might entail in the context of specific cases.

During the course of our discussions, the OECD's "Due Diligence Guidance for Responsible Business Conduct" was finalized, highlighting several factors that should be considered in determining whether a company's actions or inactions could be deemed to have made a substantial contribution to an impact in a specific case. These factors include consideration of the foreseeability of a particular impact, the degree to which an activity increased the risk of an impact occurring and the effectiveness of mitigation measures in reducing the risk of impacts occurring. The quality and effectiveness of a bank's due diligence process, or failures in that process, play a role in the analysis of these factors.

We therefore hope that our analysis of expected approaches within bank due diligence practices can play a helpful role in further conversations exploring responsibility for impacts in the financial sector – even while recognizing that additional factors would need to be considered.

2 Responsibility for Remedy Under the OECD Guidelines and the UNGPs

2.1 Cause, Contribution and Linkage

The OECD Guidelines and the UNGPs identify three different ways a business could be connected to an adverse human rights impact, with corresponding differentiated responsibilities for action in response.[1] The definitions below are aligned with these international frameworks and reflect language used by OHCHR in advice it has provided on this topic.[2]

- **Cause**: A business can cause an adverse impact where its activities (its action or omissions) on their own remove or reduce a person's or group of persons' ability to enjoy a human right, i.e., where the business's activities on their own, without other actors, are sufficient to result in the adverse impact.

  If a business has caused or could cause an impact, then the business should take steps to prevent or mitigate the impact from occurring, continuing or recurring. The business should also provide remedy for the harm (either through its own processes or by cooperating in credible external processes).

- **Contribution**: A business can contribute to an adverse impact through its own activities (actions or omissions) – either directly alongside other entities (contribution in parallel), or through some outside entity (such as another business) by facilitating or incentivizing the actions or inactions of another party that result in an adverse impact on people (contribution through a third party).[3] Contribution implies an element of 'causality', for example that a business's actions or decisions influenced another actor in such a way as to make the adverse human rights impact more likely.

1 The OECD Guidelines for Multinational Enterprises also treat impacts beyond human rights, (e.g. disclosure, employment and industrial relations, environment, combatting bribery, bribe solicitation and extortion, consumer interests, science and technology, competition and taxation); however, the scope of the Dutch Banking Sector Agreement focuses only on human rights.
2 See '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', pp. 5-6, *www.ohchr.org/documents/issues/business/interpretationguidingprinciples.pdf.*
3 See section 5.2 of this paper for the definitions.

If a business has contributed or could contribute to an adverse impact, then the business should take steps to prevent or mitigate its contribution to the impact occurring, continuing or recurring. The business should also contribute to the remedy for the harm, appropriate to its contribution to the impact taking place (either through its own processes or by cooperating in credible external processes). And finally, the business should use its leverage (and build additional leverage where needed) to seek to influence the behaviors and actions of other actors playing a role in the impact taking place.

- **Linkage**: In other situations, an impact may be directly linked to a business's operations, products or services through a business relationship with the entity causing or contributing to the impact, but without any contribution by the business itself. A business relationship with another entity that causes harm is not sufficient on its own to create linkage; rather, the impact that occurs through another entity must be linked to the business's products or services to establish this form of responsibility.

  Where linkage exists, the business should use its leverage (and build additional leverage where needed) to seek to influence the behaviors and actions of other actors playing a role in the impact taking place, in order to prevent or mitigate the impact from occurring, continuing or recurring.

  In linkage situations, the business does not itself have a responsibility to provide remedy for the harm. However, the business is responsible for taking steps to mitigate the risk of impacts through business relationships. One of the most effective ways of using that leverage is likely to include encouraging third parties to provide effective remedy mechanisms for impacts that have occurred. UNGP 19 elaborates on the appropriate action expected in linkage situations, which may include using any leverage the business may have over others to seek to influence those actors to provide for remediation.[4]

4 This relevance of remedy in linkage situations is explored in the OHCHR response to BankTrack, in the UNGPs under UNGP 19 and its commentary, as well as the UNGP Interpretive Guide, pp 48-52. Additionally, the MNE Declaration of the ILO states: 'Multinational enterprises should use their leverage to encourage their business partners to provide effective means of enabling remediation for abuses of internationally recognized human rights.' See Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy, 5th ed, March 2017, para 65. Likewise, the OECD guidance for institutional investors states that, in linkage situations, 'investors would not be expected to provide remedy, but they should seek to encourage the investee company to do so' as a component of their responsibility to seek to prevent and mitigate impacts. This is a more nuanced understanding of responsibility with regards to remedy in linkage situations, than the common shorthand explanation that businesses do not have a responsibility to provide remedy in linkage situations.

2.2 Insights That Shaped Working Group Discussions

Within the context of exploring bank responsibility and remedy, the Working Group recognized two key insights that shaped its discussions:

- **The Relevance of Remedy Across all Forms of Responsibility**: The expectations described above highlight that remedy is relevant in different ways in in cause, contribution and linkage situations. The Working Group therefore explored appropriate roles for banks in making remedy more available, across different forms of responsibility. (We explore these roles in Section 4).
- **The Relevance of Due Diligence (and Action and Inaction) in Understanding Responsibility:** These definitions of how a business can be connected to a harm highlight one of the underlying motivations of the OECD Guidelines and the UNGPs – to incentivize appropriate action by business to prevent and address harm to people they might be connected to. The expectation of due diligence asks businesses to seek to understand the risks and inform business decisions and actions with this knowledge, rather than choosing deliberately not to know. The quality and effectiveness of due diligence therefore becomes a relevant consideration in determining how a business is connected to a particular impact[5], in conjunction with other factors. The analysis of responsibility requires looking at the steps a business has taken (or failed to take) to assess and address risks[6], whether those steps were effective in actually mitigating risks or impacts, and the degree to which those actions or omissions increased the risk of the impact occurring. (In Section 5, we focus in particular on the adequacy of due diligence steps).

5 See OHCHR Response to BankTrack, p. 8: 'The bank's failure to act upon information that was or should have been available to it may create a facilitating environment for a client to more easily take actions that result in abuses. Conversely, if the bank knows about a human rights risk associated with a particular project and takes reasonable steps to prevent and mitigate these risks, the situation would instead in principle be one of 'linkage'.

6 The concept of leverage featured in this Working Group's discussions, particularly as it related to the ability of banks to assess actual and potential impacts (by gathering information about the client, the transaction, actual or potential impacts, and planned mitigation measures) and to address those impacts (through engagement with the client). However, a separate Working Group under the DBA was focused more comprehensively on exploring the barriers and opportunities for banks in building and using leverage.

3 Context for Discussing Bank Responsibility for Remedy

3.1 International Conversations on Financial Sector Responsibility

The Working Group recognizes the relevance of ongoing discussions at the OECD level, including both the OECD's cross-sector guidance on due diligence (which was completed during the course of the Working Group's discussions) and the OECD Advisory Group on the Financial Sector; the relevance of the authoritative OHCHR advice; and conversations among the Thun Group of banks, including their revised discussion paper issued in December 2017, and responses to that paper from civil society and other stakeholders.[1]

One of the unique features of this Working Group was the opportunity for banks and stakeholders to explore these questions together, in a multi-stakeholder setting, under the umbrella of the sector-based agreement. The Working Group hopes that its process and discussions can provide a useful input into these other discussion forums where similar questions are being explored.

3.2 Relevant Contextual Factors in Understanding Due Diligence in the Banking Sector

The Working Group recognized that the adequacy of due diligence can play an important role in analyzing responsibility under UNGPs and the OECD Guidelines for impacts a bank is connected to through client relationships, (see Section 2.2. above), and particularly in distinguishing situations of contribution from situations of linkage. During the course of discussions, several factors emerged that help to shape the context within which that due diligence currently takes place within the banking sector.

These include factors related to the nature of the bank-client relationship, industry context, and the practical limitations of current industry practices. Members of the Working Group recognized that these factors represent practical realities and challenges for bank due diligence, as opposed to excusing a bank from responsibility for impacts that might arise through client relationships. Working

1 Available at *https://business-humanrights.org/sites/default/files/documents/2017_12_Thun%20Group%20of%20Banks_Paper_UNGPs%2013b%20and%2017.pdf*

Group discussions explored potential opportunities to overcome some of these barriers.

3.2.1 Differences between Project Finance and Corporate Lending Contexts

Working group discussions recognized at a general level important differences between project finance and corporate lending contexts. These relate, among others, to the quantity and breadth of client relationships, the amount of visibility into client operations and activities, the role that initial risk screening and classification play in determining appropriate levels of due diligence, and the extent to which expectations are more standardized across the industry. These differences are presented as generalities in Table 3.1 below, and further explored throughout this discussion paper.

Table 3.1 General Differences in Corporate Lending and Project Finance

	Corporate lending	Project finance
Scope of Responsibility for Due Diligence	**Broad.** All actual or potential impacts related to full scope of client activities and value chains.	**More Narrow.** Only those actual or potential impacts connected to project activities or the dedicated value chain of the project. (Due diligence not required on the full range of activities of parties involved in the project (i.e., activities not connected to the specific project being financed), although some banks may extend their due diligence beyond this.
Quantity and breadth of client relationships	**Vast.** By way of illustration, the Dutch banks involved in the DBA have hundreds of thousands of corporate clients in their corporate lending portfolios.	**More Limited.** By way of illustration, the five Dutch members of the Equator Principles Association were involved in 99 projects that fall under the scope of the Equator Principles in 2016; 11 of these were classified as 'Category A' projects, which are high risk projects with severe impacts.
Standardization of expectations	**Less Standard.** Varies among individual banks. Each bank has its own policies for managing human rights and environmental and social risks.	**More Standard.** Expectations codified in the Equator Principles and IFC Performance Standards.

Risk Classification	**Varies among banks.** Banks have their own criteria for determining which clients or transactions are subjected to enhanced human rights due diligence. Criteria are often captured in a bank's Environmental and Social Risk Management (ESRM) framework (and sector-specific policies), which are intended to flag certain relationships or transactions for enhanced due diligence. These are often publicly available in summary form on bank web sites.	**Standard.** The Equator Principles have standard criteria for classifying projects as Category A, B, or C, depending on the level of risks identified in the project and whether the project is taking place in "designated" and "non-designated" countries. Specific minimum steps of expected due diligence accompany each category.
Initial knowledge	**More Limited.** Typically informed by (1) information provided by the client, (2) information that is available in the public domain, (3) information from commercial data providers. At a minimum, banks typically have information available through Know-Your-Customer (KYC) due diligence performed on all clients, which is not specifically focused on human rights.	**More Robust.** Typically informed by: (1) the same sources as in corporate lending; (2) more specific information about project activities and value chain partners presented in project plans and loan applications; and (3) standard practice for banks to require projects to provide an Environmental and Social Impact Assessment; for higher risk projects banks may also commission evaluation by their own consultant.
Timing and intensity of Due Diligence	**Varies,** depending on the bank's risk classification system. For relationships and transactions not flagged for heightened risk, there may be no additional assessment on the initial screening. For most other transactions, banks' human rights experts may typically have a few days to make an assessment of the prospective client, based on desk-top review of available information. Banks would then continue to monitor transactions (actively and passively) for indications of human rights impacts.	**Opportunities for Earlier, Longer, More Intense.** Banks' human rights experts are involved in the early stages of the investment process of new project deals. Banks taking a leading role in the syndicate will have the opportunity to have a longer and more intense due diligence trajectory. Similarly, banks would then continue to monitor transactions (actively and passively) for indications of human rights impacts. Participating banks may have limited opportunity to engage directly with the client and therefore are to some extent more dependent on the actions of the lead bank.
Expectations concerning remedy	**Varies among banks.** General bank policies may set expectation for client mechanisms for remedy. However, due to quantity of relationships and nature of corporate lending, assessing the quality of *operational-level* grievance mechanisms poses more significant challenges.	**More Clear.** Under the Equator Principles, banks are required to require clients to have effective grievance mechanisms for all Category A (and some Category B) projects in "non-designated countries". Often assessed as part of the assessment of the environment and social management system (ESMS).

3.2.2 Prioritizing Relationships for Enhanced Due Diligence

Particularly in the context of corporate lending, banks may have more than tens of thousands of relationships to business clients, and exponentially more through their clients' value chains, spread across a broad range of sectors and countries. Just as large businesses in other sectors may not be able to conduct in depth due diligence across the entirety of their value chains, a bank is likely unable to conduct the same level of due diligence across the entirety of its client relationships.

Prioritizing client relationships on which to focus due diligence may be challenging for banks, due to the amount of information and visibility a bank might typically have into client operations and activities. This may depend on the type of financial service or product and the nature of the client relationship. Under current practice banks often do not have access to the necessary information at scale about all client business relationships and activities, in order to make informed choices about which clients (or specific subsidiaries or activities of clients) to prioritize for enhanced due diligence.

The context for project finance is different, in that banks deal with a more manageable set of client relationships, more visibility into client operations, greater leverage with clients to gather additional information, and more standardized systems and expectations for risk categorization and corresponding levels of due diligence for each transaction. However, it also has its own challenges, for example, that impact assessments and even community engagement processes have often already been completed by the time that financiers are involved.

3.2.3 Timing

Issues of timing can play an important role in the practical realities of bank due diligence in several different ways. In some instances, banks may find themselves in situations with limited time to conduct due diligence before making a business decision to provide or participate in a financial relationship. In other instances, the banking relationship may be established before all impacts have occurred or can be known, or before local communities have the capacity to raise their concerns. Each of these timing realities may create practical constraints on the type of due diligence banks are able to conduct in different circumstances.

3.2.4 Syndicated Loans[2]

Certain types of financial products or services may put banks in a position of relying upon other actors to inform their individual due diligence processes. Syndicated loans, in particular, came up a number of times in case discussions, where participating banks may face additional hurdles in their ability to conduct due diligence. In a syndicated loan, banks take different roles, such as lead arranger, book-runner, agent or participant. Depending on the way those roles are structured, different roles may create greater and lesser opportunities for direct engagement with the client, in order to gather the necessary information to assess risks or to use leverage with clients to seek to address risks. As one illustration, conditions in the loan documentation for syndicated facilities (such as the ability to inspect a client's premises) can often only be triggered when there is majority consent of the banks participating in the syndicate, which may make it more challenging for an individual bank to conduct the type of due diligence it deems appropriate without the agreement of the other banks.

3.2.5 Legal and Regulatory Constraints

Laws and regulations, including those on client confidentiality and anti-competition laws, may create different circumstances for banks with respect to the scope of engagement with stakeholders, other expert resources and peer banking institutions. This may be relevant in the process of assessing and addressing risks, or in the process of communicating about the bank's performance on human rights.[3]

3.2.6 The Nature of Financing

The OECD Due Diligence Guidance states that 'the mere existence of a business relationship or activities which create the general conditions in which it is possible for adverse impacts to occur does not necessarily represent a relationship of contribution. The activity in question should substantially increase the risk of the adverse impact.' The group discussed differing views on how this statement would apply in practice within the context of the financial sector. Is financing different in kind from other types of inputs into a business activity (such as raw materials or supply chain components)? Does financing play a more essential role in enabling business activities to proceed than other forms of inputs? If so, to what extent does this challenge the definitions of key terms in the OECD Guidelines for

2 Syndicated loans, also known as a syndicated bank facility, is a loan offered by a group of lenders that work together to provide funds for a single borrower, which could be a corporation, a project, or a sovereign government.

3 A separate work stream under the Dutch Banking Agreement explored the limitations and opportunities posed by client confidentiality requirements, see for the results *https://www.imvoconvenanten.nl/banking/news/2018/5/human-rights-policy?sc_lang=en.*

understanding responsibility for impacts, such as ‘facilitating’, ‘enabling’, ‘substantial’ and ‘non-trivial’? In what ways does the fungible nature of money, particularly in corporate lending, challenge interpretations about the extent and limitations of responsibility for impacts connected to a product or service, when considering a general financial product that enables a broad range of business activities to proceed?

3.3 The Remedy Gap

The UNGPs and OECD Guidelines recognize that, regardless of the quality of due diligence processes, adverse human rights impacts may occur, and that when those impacts occur, people who are harmed should have access to remedy. Members of the Working Group observe that, globally, there remains a significant remedy gap in practice. This is a general observation, not distinctive to Dutch banks or even to the financial sector alone. However, the reality remains that in many cases where severe negative impacts occur, remedy is often not available to individuals and groups suffering harm connected to business activities.

Working Group discussions have sought to close that gap in two ways: (a) by creating a shared understanding of the circumstances under which a bank has responsibility to address that gap directly by providing or contributing to remedy for the harm that occurred, or to use its leverage to seek to enable remedy provided by other parties, recognizing that the specific responsibility of a bank with regard to remedy will depend on how the bank is connected to the impacts; and (b) by exploring ways to strengthen the practices of banks in enabling remedy in each of these circumstances. The latter will be discussed in the following chapter.

4 Enabling Remedy: Roles for Banks

Framing Question: *What types of actions could a bank take, and what appropriate roles could a bank play, to enable remedy more effectively in practice, recognizing that the specific responsibility of a bank with regard to remedy will depend on how the bank is connected to the impact?*

4.1 The Relevance of Remedy Across All Forms of Responsibility

The members of the Working Group jointly recognized that remedy is a relevant consideration in all cases in which a bank is connected to a negative impact, across all forms of responsibility. In situations of linkage, banks have a responsibility to use and build their leverage to seek to influence the actions of other parties that may have caused or contributed to the negative impact, including by seeking to enable remedy through the actions of their clients. In situations of contribution, banks have a responsibility to use and build their leverage with other responsible parties, but also to contribute to that remedy themselves.

This part of the paper explores a number of specific actions banks could take to address the remedy gap in practice – by supplementing the question of who is responsible for providing remedy with an exploration of practical actions banks could take to enable remedy. Discussions of the Working Group recognized significant opportunities to strengthen current bank practices when it comes to meeting these various forms of responsibility with regard to remedy – many of which can be acted upon immediately, even while discussions continue around contribution and linkage.

4.2 Re-Thinking Roles in Remedy: An Eco-System Approach

In exploring these practical approaches, the Working Group found it helpful to think about the roles banks could play in a broader 'remedy eco-system'[1] (discussed in greater detail below), where different actors have different but complementary roles to play in the remedy conversation. Although the Working Group found this eco-system approach helpful in extending the conversation, it should not imply any

1 Shift has been exploring the concept of the remedy ecosystem in its work with business and financial institutions and introduced the concept into WG conversations. See: *https://www.shiftproject.org/resources/viewpoints/rethinking-remedy-responsibility-financial-sector-ecosystem-human-rights/*

attempt to shift the individual responsibility of a bank in situations where a bank is contributing or directly linked to an impact.

The specific actions and roles explored in this paper are not intended to be prescriptive. They should not be read as steps every bank must take to meet their responsibility. Both the UNGPs and the OECD Guidelines allow for substantial flexibility in how institutions might seek to meet the expectations outlined in the guidelines. Indeed, the specific steps that may be available or appropriate for a bank to take in a specific situation will depend on a number of factors, including the type of financial relationship that connects a bank to an impact, the types of leverage the bank may have, and the roles being played by other relevant actors.

Nevertheless, the Working Group recognizes the need and opportunity for banks to bring a greater focus to making effective remedy available when connected to impacts, and hopes this part of the paper offers practical approaches for how banks could do so in practice.

The sub-sections that follow explore:
- Current practices and conversations around financial institutions and remedy, and the need to shift the approach (section 4.3);
- Definitions of severe key concepts relevant to remedy, and some foundational assumptions that shape the approach explored by the Working Group (section 4.4);
- The key features of understanding roles and responsibilities in remedy through the lens of an eco-system approach (section 4.5); and,
- Specific actions banks could take in practice to ensure (i) preparedness for remedy before impacts occur; and (ii) actions to support remedy after impacts have occurred (section 4.6).

4.3 Current context for Banks and Remedy: The Need to extent the Conversation

Several broad observations informed the Working Group's exploration of the role of banks in enabling remedy in practice:
- **Much of the conversation around banks and remedy is currently focused on grievance mechanisms**, which are related to, but distinctive from remedy (see section 4.4). For many banks and financial institutions, their approach to remedy is based on requiring their clients to have operational-level grievance mechanisms at the project or client level. Assessing whether such mechanisms

exist is often included as part of a bank's environmental and social due risk management process.[2] As far as the Working Group knows, there are no examples of private commercial banks having grievance mechanisms in place for the impacts connected to the activities of their clients.[3]

- **When allegations of specific impacts do arise, banks often find it challenging to focus the conversation on a holistic approach to remedy**. Banks will typically engage with their clients to better understand the situation, and push the client to take action to address the issue. However, if a company disputes the allegations, banks are both geographically distant from where impacts occur and may not have the allocated investigative resources to establish facts on the ground. As a result, in responding to specific impacts, many banks and financial institutions tend to push clients for forward-looking changes to company policy or practice, in order to prevent future similar impacts, rather than remedy for specific affected stakeholders who have been harmed in a specific case.
- **At a policy dialogue level, financial institutions and stakeholders are focusing primarily on the question of responsibility for providing remedy, rather than practical actions to enable remedy**. These two are related, but different. Across various forums, discussions are more focused on understanding when a bank might be causing, contributing, directly linked, or not connected to an impact through corporate lending relationships. Much less discussion is taking place around practical approaches banks can take to enable access to remedy in practice, either in contribution or – in particular – in linkage situations.

The current focus of these conversations is therefore missing an opportunity to more fully explore the practical steps that banks could take around remedy, even as discussions about responsibility should continue. The Working Group therefore recognized a significant opportunity to contribute to better outcomes for people in practice, by supplementing the conversation:

- From focusing solely on when a bank has a responsibility to provide remedy, to focusing on **practical approaches banks can take to enable remedy across all forms of connection**, including through the use of leverage;
- From focusing primarily on grievance mechanisms at either the client or bank level, to a focus on **supporting an effective remedy eco-system** – which includes, but is not limited to, those client and bank-level mechanisms; and,

2 See OHCHR response to BankTrack: "banks are expected to have mechanisms in place (their own or one they participate in) to respond effectively if or when grievances arise"

3 Practice is different among public financial institutions, such as the IFC or FMO in the Netherlands, or among some export credit agencies including Atradius DSB in the Netherlands, where grievance mechanisms or complaints processes at the bank level are becoming more of a common and established practice.

- From a limited set of current practices when impacts occur to a **more expansive toolkit** of potential ways a bank might better prepare for the potential need for remedy and ways a bank could use its leverage to bring a greater focus to remedy in specific cases.

4.4 Defining Core Concepts

The Working Group's approach is based on a shared understanding of several key terms, which are defined in this section: (1) remedy, (2) grievance mechanisms, (3) grievance mechanism infrastructure, and (4) remedy eco-system.

4.4.1 Remedy

When human rights abuses occur, those who are harmed are entitled to effective remedy. The idea of effective remedy is that those individuals or groups who have suffered some adverse impact to their human rights should be made whole again, by restoring them to a situation the same as or as close as possible to the position they were in before the impact occurred. The actual measures of reparation will depend on the nature of the harm suffered and the wishes of those adversely impacted.[4]

- Remedy is multi-faceted, in that its objective can have **preventive, redressive and deterrent elements**. Preventive refers to ensuring that the harm ceases and does not continue or recur. Redressive refers to seeking to restore affected individuals or groups to the same or or as close as possible to the situation they would have been in had the impact not occurred in the first place; i.e. making them "whole" again. Deterrent refers to creating an incentive for parties that might cause a negative impact to avoid causing that impact in the first place.

- Remedy can therefore take many forms, including (combinations of): restitution, compensation, rehabilitation, satisfaction, guarantees of non-repetition, apology, punitive sanctions, or other preventive measures.[5] Effective remedy may require **a holistic approach**, including multiple elements from this list.

4 See UN Guiding Principles on Business and Human Rights and UN Human Rights Council, *Human rights and transnational corporations and other business enterprises: note by the Secretary-General, 18 July 2018,* A/72/162

5 Examples from an expert of the WG on forms of remedy include restitution in the *Wilmar case at the CAO* where the communities got land back, compensation in the *Dutch NCP complaint against Heineken,* in which ex-workers received monetary compensation and satisfaction in the *Dutch NCP complaint against Nidera,* in which working conditions improved.

- Effective remedy therefore requires **a stakeholder-centric approach**, in order to understand which elements are essential for an effective remedy from the perspective of those who have been harmed.

4.4.2 Grievance Mechanisms

Grievance mechanisms are processes established to allow affected stakeholders to raise complaints or concerns with relevant parties and to have those complaints or concerns addressed and resolved.

- Grievance mechanisms include a range of different types of institutions and processes. They can be state-based and non-state-based; judicial and non-judicial, adjudicative or more dialogue-based. They can include national court systems; regulatory bodies such as national human rights institutions, ombudsman, or labor inspectorates; project or company-based; or connected to industry associations or multi-stakeholder initiatives.

- The UNGPs identify 8 effectiveness criteria for non-judicial grievance mechanisms, as the characteristics that should guide the design and implementation of effective grievance mechanisms: legitimate, accessible, predictable, equitable, transparent, rights-compatible, source of continuous leaning, and (in the case of company mechanisms) based on dialogue.[6]

- Effective grievance mechanisms can play a variety of different roles, including: (a) providing remedy to stakeholders; (b) serving as a feedback loop as part of ongoing company due diligence, by identifying actual impacts (as opposed to risks) and as an indication of the effectiveness of prevention and mitigation measures; and (c) holding companies accountability for commitments made.

- Under the UNGPs, businesses, including individual banks[7], have a responsibility to establish or participate in effective operational-level grievance mechanisms.

4.4.3 Grievance Mechanism infrastructure

Ideally, in any given context, a number of potential pathways for remedy, or grievance mechanisms, may be present. However in practice, affected stakeholders have very few options available to them to seek remedy.

6 See: *https://www.business-humanrights.org/sites/default/files/media/documents/ruggie/grievance-mechanism-pilots-report-harvard-csri-jun-2011.pdf.*

7 OHCHR response to BankTrack: 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'.

In the case of an impact, stakeholders might raise their concern and seek remedy through national court systems, regulatory or administrative bodies, community-level mechanisms, project level mechanisms, site-based company mechanisms, corporate-level mechanisms, institutions in the country context where the impact took place or in the home country of the company's headquarters (including National Contact Points for the OECD Guidelines and home state courts), mechanisms of financing institutions, or others – including ad hoc processes established to address specific situations after they have arisen.

The Working Group understands grievance mechanism infrastructure to refer to the totality of these potential pathways for remedy, from the perspective of an affected stakeholder. Each mechanism will have its own strengths and weaknesses in any given context, and each may be better or less well equipped to provide certain types or elements of remedy.

4.4.4 Remedy Eco-System

The Working Group understood the concept of a remedy eco-system approach to mean a focus not only on the grievance mechanisms that can be pathways for remedy, but also the roles and responsibilities that a broad range of relevant actors might play to ensure that affected stakeholders have access to remedy in practice. For example, in addition to the various grievance mechanisms that may be available to affected stakeholders, actors such as banks, investors, or business partners may need to use their leverage with responsible parties to influence them to provide remedy. Likewise, civil society advocates (including local or international NGOs or trade unions) who might help individuals or communities frame their complaints and support their effective participation in remedy processes would likewise be part of the remedy eco-system. In short, the remedy eco-system incorporates all the mechanisms, actors, roles and responsibilities that may be necessary to enable remedy in practice.

4.5 Giving Shape to an Eco-System Appraoch

4.5.1 Why a remedy eco-system?

A remedy eco-system approach is intended to bring the focusto outcomes for affected people, rather than focusing narrowly or solely on the question of who is responsible for providing remedy and whether or not grievance mechanisms exist.

The eco-system approach seeks to recognize that:

- enabling remedy may require action by all parties that have caused, contributed to or are directly linked to the harm;
- Ensuring grievance mechanisms are present is not likely to be sufficient to enable remedy in practice in many cases, nor does it necessarily meet the remedy responsibilities of parties by itself;
- There is a difference between having a grievance mechanism and enabling remedy in practice. Grievance mechanisms are formal processes that, when working effectively, can enable remedy. But remedy is the act of making affected stakeholders whole again;
- When impacts occur, parties connected to that impact have a responsibility to take action to address those impacts, including by focusing on remedy, whether or not those grievance mechanisms are present, effective or utilized;
- Affected stakeholders may in many cases need different forms of support to access and participate effectively in processes to enable remedy;
- That a variety of actors, including businesses connected to the impact, governments, civil society organizations and trade unions may have various complementary and supporting roles to play to enable remedy in practice.

Under the OECD-Guidelines and the UNGPs, businesses, including banks, have an individual responsibility with regard to remedy depending on how the business is connected to the impact. The eco-system enables banks to exercise this individual responsibility. What the individual responsibility is of a bank and the variety of roles it can play within an eco-system will depend on the connection to the impact.

4.5.2 Recognizing different components of a robust grievance mechanism infrastructure

In any operational context where an impact occurs, a number of potential grievance mechanisms or pathways may be present. For example, there may be a national court system, a project or site-level company grievance mechanism, a National Contact Point for the OECD Guidelines located in the host state or the home state of the company in question, and some form of a bank-level mechanism. Each of these may have specific advantages and disadvantages, depending on how they are designed and how they operate in practice. For example:

- A national judicial system may be best-placed to adjudicate facts, allocate accountability, and compel certain forms of remedy, such as punitive sanctions, injunctions, or financial compensation. However, the process may be slow, resource-intensive, or not trusted by all stakeholders.

- A project or site-level company mechanism may be more accessible to affected stakeholders and capable of providing more immediate outcomes, as well as a more tailored and wider range of potential outcomes, but may place disproportionate decision-making power in the hands of the company, to investigate and adjudicate complaints about its own actions, and may therefore be dependent on the company's willingness to accept responsibility and determine appropriate outcomes.
- A National Contact Point (NCP)[8] can offer an independent third-party mediation and conciliation platform for resolution of issues that has jurisdictional flexiblity and might be less expensive and faster than legal proceedings, but will likely face challenges of accessibility for affected stakeholders, may have limited investigative powers, lack clear adjudicative powers, and therefore require the voluntary participation of the parties responsible for causing the harm. While an NCP has the power of the State behind it, it is a mediation and conciliation platform and therefore cannot compel a company to take actions on remedy that the company does not agree to.
- Likewise, a bank-level mechanism (either at the level of an individual bank or a sectoral or cooperative mechanism) could play a particularly useful role in the bank's own due diligence, by informing the bank of actual impacts that were not effectively assessed or managed, and by alerting the bank to situations where the client-level mechanisms were not operating effectively in practice for one reason or another. In situations where a bank has contributed to an impact, a bank-level mechanism could also provide a clear pathway for the bank to contribute to remedy. However, a bank-level mechanism is likely to face challenges of accessibility, in terms of both its remoteness and whether stakeholders will be aware of who is financing a project or company. A bank-level mechanism may also face challenges in delivering actual remedy, where other parties are involved in causing a harm. Such a mechanism would require some degree of commercial, contractual, or relationship-based leverage in order to compel the participation of those parties that caused the harm in both remedy processes and outcomes.

Different mechanisms should play different but complementary roles, as part of a robust infrastructure. Different mechanisms may be more appropriate for different affected stakeholders, in different circumstances, depending on the

8 NCPs are agencies established by adhering governments to promote and implement the OECD Guidelines for Multinational Enterprises (the Guidelines). NCPs assist enterprises and their stakeholders to take appropriate measures to further the implementation of the Guidelines. They also provide a mediation and conciliation platform for resolving practical issues that may arise. See OECD Guidelines for Multinational Enterprises (2011), Foreword

particular form of remedy that is sought. However, where one of these levels of the infrastructure is weak or non-existent, it may place greater strain on other mechanisms within the eco-system, expecting those mechanisms to play roles they are not well-suited to play. Ideally, for an effective robust infrastructure all grievance mechanisms need to be in place. The existence of one cannot be a reason for the absence of another.

4.5.3 Assumptions about remedy and grievance mechanisms

The Working Group's understanding of how banks might play constructive roles in a remedy eco-system is grounded in several **foundational assumptions about remedy and grievance mechanisms**, based on the experience of participants and experts in the Working Group:

- That remedy is more likely to be effective and sustainable when the process is stakeholder-driven, informed and guided by the perspectives and desired outcomes of those who have been negatively affected.
- Ideally, remedy would be provided locally, as close to the source of the impact as possible. Local grievance mechanisms – where effective – are most likely to be the most accessible to affected stakeholders, and most likely to involve the relevant and responsible parties when it comes to remedy. However, in some cases remedy is best provided elsewhere.
- That remedy is likely best provided when the parties responsible for causing or contributing to the impact, and therefore with a responsibility to provide or contribute to remedy, participate constructively in the grievance process. This is particularly true for more voluntary remediation mechanisms, such as NCPs and corporate grievance mechanisms, but equally true in other ways for compulsory processes, such as court proceedings, criminal investigations, or administrative procedures.
- That different grievance mechanisms can play different roles in a remedy eco-system and are capable of providing different forms or types of remedy[9].

The Working Group's conclusion, based on all of the points raised above, is that while a bank's specific responsibility for providing, contributing to, or enabling remedy will depend on how the bank is connected to the impact, **there are important and under-explored roles for banks to play in enabling remedy across all forms of connection**.

9 For example, an adjudicative state-based process may be capable of providing clear public rebuke; an adjudicative state-based process or a process that the company causing the harm consents to could result in specific actions by the company, such as cessation of a business activity causing harm, reinstatement of a wrongfully terminated worker, or compensation to a community or individual. However, apology is only likely possible in a meaningful way through a process the company causing the harm consents to. A bank-level mechanism might be particularly appropriate if the remedy sought is changing the due diligence or business practices of the financing institution.

Challenges in Practice: Banks, Clients and Obstacles to Remedy

In practice, banks can face a number of challenging situations where it may be difficult to navigate appropriate roles in enabling remedy. The bank's relationship is with the client, and the bank is not likely to have presence on the ground, where impacts are alleged to have occurred. The first course of action for most banks will be to engage with the client around the alleged impacts. But clients and affected stakeholders do not always see things the same way.

- Disputes over facts: The client either denies that an impact occurred, denies that people were harmed, or denies that its actions were connected to the harm.
- Disputes over who suffered harm: The client and affected stakeholders may disagree over the scale of the impact, in terms of how many people suffered the harm, and who specifically suffered the harm.
- Disputes over completeness of remedy: The client may be willing to take forward-looking steps to prevent future harm, which may be one component of remedy, but not backward-looking steps to make whole the individuals or groups who allege that they have been harmed already.
- Disputes over satisfaction with remedy: The client has provided a remedy, but there are signs that stakeholders are dissatisfied with the adequacy of that remedy.
- It's in the hands of the lawyers: The client is unwilling to discuss remedy options due to a pending legal case.

These realities framed the Working Group's discussions, and informed some of the potential actions identified.

4.6 Exploring Potential Bank Roles in a Remedy Eco-System Approach

The Working Group explored a range of potential ways that banks could bring a greater focus to remedy in practice under this eco-system framing.
These are presented below as exploratory options, and should not be seen as prescriptive advice.[10] The specific roles that would be appropriate to any given bank in a specific situation, and how a bank might implement any of these ideas in practice, would depend on a number of factors, including the nature of the financing relationship and the type of leverage the bank has or could build. The

Working Group also recognizes that many of these ideas would require further development to be actionable. However, the Working Groups hopes that by sharing these ideas for action here it can help to catalyze further conversations with a focus on action, remedy and outcomes for affected people.

The actions explored by the Working Group included actions banks could take before impacts occur, as part of preparedness for remedy, and after impacts occur, to enable remedy in the context of specific impacts and – in cases where the bank contributed to the harm – should be contributing to the remedy.

4.7 Preparedness for Remedy (Before Impacts Occur)

Before impacts occur, there are a number of actions banks could take as part of existing due diligence processes to be better prepared for remedy if impacts should ultimately occur. These include (1) supporting a robust grievance mechanism infrastructure; (2) Targeting effective due diligence for potential remedy; and (3) building leverage up front for remedy.

4.7.1 Supporting a robust grievance mechanism infrastructure

Banks can take steps at the outset of client relationships to strengthen the remedy pathways that will be available to stakeholders if impacts should occur. Some banks already demonstrate good practices in these areas, which could be built upon.

a. **Better prioritization** of relationships where grievance mechanisms are likely to be important. In practical terms, banks will not be able to focus on clients' grievance mechanisms across the entire breadth of client relationships. Banks - either individually, collectively, or collaboratively with stakeholders – could develop criteria to more accurately determine which client relationships would be most important for effective remedy mechanisms or clear approaches to remedy to be in place. This is particularly important for corporate lending relationships, as opposed to project finance, where expectations around grievance mechanisms are more standardized. For example, many banks already work with sector-based approaches to environmental and social due diligence. These could be built upon to recognize more specifically where grievance mechanisms might be most relevant.

10 Members of the Working Group did not always agree on whether a specific action was something a bank 'could' do or something a bank 'should' do. In order to present the full range of ideas explored, the entirety of this section takes the more exploratory tone of actions banks 'could' take, recognizing that some stakeholders believe these actions are expectations rather than options in meeting responsibilities under the UNGPs and the OECD Guidelines.

b. **Better assessment of effectiveness** of client-level grievance mechanisms and the broader grievance mechanism infrastructure. Banks – either individually, collectively, or collaboratively with stakeholders – could develop much better diagnostic questions to assess the effectiveness in practice of client grievance mechanism, as opposed to their existence – including mapping where different types of affected stakeholders could reasonably turn for specific types of grievances to be addressed. As part of its discussions, the Working Group gathered some of these diagnostic questions from participants and experts, and these are presented in Box 1.

Box 1

Examples of Diagnostic Questions: Assessing Effectiveness of Grievance Mechanisms

Scope:	What % of assets have a GM that is aligned with the UNGPs?
Measuring:	How many repeat grievances have been filed? What other KPIs are tracked (and reported)?
Remedy:	Did the company provide or enable remedy for any actual impacts, and if so, what are typical or significant examples? How does the company know if affected stakeholders (i.e., users and intended users) are satisfied with the process and/or the outcomes?
Management:	Is there an oversight body that reviews trends in the types of complaints that are filed, in order to identify and address root causes?
Learnings:	What are the trends and patterns in complaints or concerns and their outcomes, and what lessons has the company learned?

In Annex 1 the Working Group provides more examples of diagnostic questions based on previous work from Shift and Triple R Alliance.

c. **Better support to strengthen the effectiveness in practice of client-level grievance mechanisms.** Where banks identify priority client relationships for effective grievance mechanisms or remedy processes, but capacity at the client level is lacking, banks could – individually, collectively, or collaboratively with stakeholders – provide resources to those clients to support more effective implementation in practice. For instance, this could lead to a shared toolkit as a resource for client companies around effective grievance mechanisms or remedy processes, a list of existing good practice guidance, or a list of trusted external experts a client could turn to in order to strengthen their grievance mechanism.

d. **Identifying and strengthening complemetary mechanisms.** Part of a robust grievance infrastructure is the availability of multiple mechanisms, in case the client-level mechanism is not an effective or chosen path for affected stakeholders. These could include state-based mechanisms, industry mechanisms or bank-level mechanisms. Banks could play a role in ensuring or advocating for such mechanisms to be designed to play complementary and supportive roles to each other, recognizing their role in the broader infrastructure and eco-system.

4.7.2 Targeting effective due diligence for potential remedy

Effective due diligence prior to impacts occurring can play a significant role in ensuring preparedness for remedy, in case impacts occur as business activities unfold. For those relationships that are determined to pose heightened risk for severe impacts, the due diligence might specifically focus on areas that are particularly relevant to remedy, namely:

a. **The quality of stakeholder mapping:** if impacts should occur, does the company have an adequate understanding of potentially affected stakeholder groups?
b. **The quality of the risk assessment**: has the company done an adequate job of anticipating which types of impacts are most likely to occur, in order to design grievance processes effectively for addressing those impacts and those stakeholders most likely to be affected?
c. **Client commitment and capacity for remedy:** Banks could communicate expectations about remedy more clearly up front, and then as part of its due diligence assess the client understanding, capability and commitment to meeting those expectations.

4.7.3 Building leverage up front for remedy

The Working Group identified several potential avenues for banks to build greater leverage up front for remedy, should impacts occur later, some of which reflect existing practices, while others are far more exploratory.

a. **Information Requirements:** Many banks include in their contractual agreements standard clauses requiring the client to notify the bank of certain serious incidents. This approach could be built upon to include severe human rights impacts in general, or a specific set of risks or impacts based on the company or bank's risk assessment.
b. **Inspection Requirements:** Many banks include standard clauses in their contractual agreements providing the bank with a general ability to inspect operational areas and the specific ability to send a third-party consultant in the case of a significant adverse impact of some kind.

c. **Commitment to address impacts:** Banks could include standard clauses obligating a client to take specific mitigation measures to address specific severe human rights impacts that had been identified as risks in due diligence process, should they occur, including agreed upon processes for enabling and / or providing remedy.
d. **Client participation:** If a bank has established a bank-level grievance mechanism, a bank could build its leverage up front to ensure (or enforce) the good faith participation of clients in complaints brought to the bank that involve the client.[11] Similarly, banks could establish codes of conduct for banks and their clients – perhaps at an industry level – when faced with official court proceedings relating to severe human rights impacts.
e. **Bank participation:** Banks could play more substantive roles in third-party grievance mechanisms, including serving on oversight, monitoring, or steering groups, whether they are those of their clients (which may be challenging in practice except in project finance contexts) or more likely at an industry level, for example, in the grievance processes of commodity-based certification schemes, such as the Roundtable on Sustainable Palm Oil.
f. **Policy commitment for remedy:** Banks should begin to include specific commitments in their human rights policy statements, in terms of articulating their approach to remedy – including how they would intend to use their own processes, how they would participate in others' processes, how they would cooperate with authorities in the case of legal proceedings against a client, what they expect from their clients and how they would intend to use their leverage for remedy if impacts should occur.[12]
g. **Resources for Remedy:** Banks could explore ways to standardize an approach to ensuring that clients will have appropriate resources available for remedy, should impacts occur.
h. **Grounds for Disengagement:** Banks could include in their policy commitments more transparency around criteria for disengaging with a client, specific to the client's good faith efforts to participate in remedy processes if impacts should occur and more clarity on the criteria for disengagement in their contractual clauses.
i. **Transparency clauses:** Banks could explore options, at a national regulatory or industry level, to have superseding transparency clauses, which would waive

11 FMO and DEG introduced such clauses for the shared Independent Complaints Mechanism developed in 2014. However, the Working Group notes important market differentiators between public development finance institutions and private commercial banks that would need to be explored further.
12 See Finnfund's statement: *https://www.finnfund.fi/wp-content/uploads/2019/01/Finnfund-Human-Rights-Statement_Final-ENG_230119.pdf*; and EDC's policy: *https://www.edc.ca/content/dam/edc/en/corporate/corporate-social-responsibility/environment-people/human-rights-policy.pdf*

client confidentiality requirements in case of severe or gross human rights impacts, recognizing that these definitions would need to be further explored and specified.

j. **Syndicated Loans:** Banks could ensure that these types of practices are included as standard practice in syndicate financing arrangements, in addition to their own lending activities.

4.8 Remedy in Specific Cases (After Impacts Occur)

There are several roles and tools banks can deploy to bring a focus to remedy after impacts have occurred. Banks will not be able to use all of these tools in all cases, and may need to prioritize on the basis of the severity of the harm. The ability of a bank to play these roles or use specific tools may depend on the extent to which steps were taken earlier to ensure preparedness for remedy, or the extent to which the bank has or can build leverage.

4.8.1 Roles Banks Could Play After Impacts Occur

The Working Group identified several roles that banks could play when impacts occur or are alleged to have occurred.[13] The fulfilment of these roles often involves consultation with the client as a first step.

a. **Clarifying the facts:** Identifying which stakeholders suffered what harm, from which business activities, and what the underlying root causes of the harm were.
b. **Focusing client attention on remedy:** Raising the issue of remedy with the client, helping the client to understand its responsibility for remedy and the meaning of remedy as needed, and ensuring that remedy for negatively affected individuals and groups is a priority for the client.
c. **Ensuring affected stakeholder voice in remedy conversations:** Assessing the role of affected stakeholders in remedy processes and ensuring that rightsholder perspectives are central in the remedy conversations.
d. **Ensuring quality of process:** Paying special attention to remedy processes to ensure effectiveness.
e. **Monitoring implementation of remedy outcomes:** Holding companies accountable for remedy actions that might be agreed to, to ensure that remedy is delivered in practice.

13 The Fair finance Guide, in which a.o. Amnesty International Netherlands, Oxfam Novib and PAX form a partnership, sponsored the development of a set of indicators to assess the quality of a financial institution's response to human rights abuses. They are available at https://eerlijkegeldwijzer.nl/media/494458/10-2018-po-mensenrechten.pdf (chapter 2)

f. **Contributing resources for remedy:** Where the bank has itself contributed to the harm, it would be expected to provide for or cooperate in the remediation.
g. **Urging to cooperate in good faith with any ongoing, external processes:** If a client is subject to external third-party process (see also 4.8.3), the bank could apply leverage to its client to cooperate in good faith with this process

The ability of a bank to play all the above-mentioned roles depends on the circumstances. In cases where a bank identified that it has contributed to an adverse impact, it has an individual responsibility to contribute to remedy. In these cases, it should fulfil this responsibility. Bank contributions to remedy can take many forms, including any of the approaches referenced above. Even where clients are providing remedy, a bank may contribute to or cooperate in the remediation. For example, by acknowledging to those affected its role in the harm.

4.8.2 Tools Banks Could Use After Impacts Occur

In playing these various roles, the Working Group identified a number of tools banks could use to bring a focus to remedy after impacts have occurred.

a. **Power of the question:** asking clients about impacts and approaches to remedy can itself be a powerful tool. Often, questions from investors and financiers can play a significant role in strengthening the internal leverage of those responsible for human rights or social impacts within companies.
b. **Asking for substantiation:** asking clients for details about the processes they followed in providing remedy, and evidence they can show that certain key parameters were met.
c. **Asking the affected stakeholders:** asking stakeholders what kinds of remedy they are seeking, and whether they are satisfied with the company's process.
d. **Triangulating with other parties:** testing the bank's own assessment, and the perspectives of company and stakeholders, with third parties, including local NGOs, embassies, and other partners.
e. **Independent verification:** (proposing the client to) hiring a third party consultant to engage directly on-site with the client and/or affected stakeholders to assess the situation and monitor process, progress and implementation.
f. **Process support:** facilitating the involvement of a neutral third party or mediator, by requiring the company to hire one, by recommending one, or by funding one.
g. **Collaborate:** seek to increase leverage by collaborating with other interested actors as needed, including other lenders, investors, pension funds, NGOs, government actors, and business partners.

h. **Potential for divestment:** Where parties are unwilling to play appropriate roles in remedy in good faith, disengagement – and the threat of disengagement – can be a powerful form of leverage in some cases. Divestment can be a part of remedy in some cases, if the decision is made in consultation with affected stakeholders and made public. Where banks do choose to divest, they should recognize that if they have contributed to the impact, they will continue to have a responsibility to contribute to remedy.

4.8.3 Cooperating in external processes

Members of the Working Group recognized that banks can face challenges in using their own leverage for remedy when complaints are raised through certain grievance pathways, such as judicial processes. Once formal, adjudicative fact-finding processes have been initiated, it can be more difficult for banks to engage with clients in general, and specifically, to push clients to provide remedy before judicial processes have reached a conclusion. However, banks can still use their leverage to encourage clients to seek consensual resolution with the other parties, and to cooperate in good faith with third-party processes. In cases where the bank is a party to such an external process, it should also cooperate in good faith.

5 Assessing the Nature of a Bank's Responsibility for Remedy (Contribution and Linkage)

Framing Question: *How is a bank deemed connected to adverse human rights impacts in connection to their corporate lending and project finance activities? In other words, under what circumstances might a bank contribute to negative impacts on people, and under what circumstances might a bank be directly linked to those impacts?*

The Working Group explored situations in which banks might be connected to adverse human rights impacts through their client relationships. Discussions did not explore situations in which a bank's activities caused an adverse impact (such as an impact on a bank's own employees resulting from human resources policies or practices), because the scope of the DBA is on project financing and corporate lending. These are situations where an intermediary party, for example clients or project partner, would be causing the harm.

As a result, discussions were focused on the distinction between 'contribution through a third party' (where a bank's actions or inactions facilitate or incentivize a third party to take action or fail to take action that leads to an adverse impact) and 'linkage' (where a bank's actions or inactions do not facilitate or incentivize a third party to take action or fail to take action, but an impact that can be linked to the banks activities nevertheless occurs). This distinction shapes the nature of the responsibility of the bank to contribute to remedy itself, or use leverage to seek to enable remedy by other parties.

Under the definitions of the OECD Guidelines and the UNGPs, 'cause' would not be relevant in such situations, because of the role of an intermediary party causing the harm. 'Contribution in parallel' is raised as potentially relevant in the context of syndicate loans, where a bank might take action or fail to take action in parallel with other banks.

5.1 Methodology: Case-Based Analysis

The Working Group used a case-based approach to building a shared understanding of the responsibility of banks with regard to remedy, with the specific facts of different scenarios providing a shared basis for discussion and analysis of responsibility.

Disclaimer regarding the cases: These fictional cases were deliberately constructed via a collaborative process by all parties. The fact patterns are not based on the current due diligence practices of Dutch banks, nor were they intended to. Rather, they were designed to facilitate discussion around the analytical process of exploring a bank's responsibility for impacts it might be connected to through client relationships and highlight factors that might be relevant to that analysis.

Specifically, the case-based discussions provided an opportunity to:

- Explore practical steps a bank might be expected to take to prevent such a situation from arising in the first place, as well as the practical steps a bank might take and the roles a bank might play if such a situation did arise;
- Change different facts within the case within the course of discussion, as a way to explore how different facts might influence the analysis of the bank's responsibility;
- Highlight practical limitations of what can be expected given current industry practice;
- Explore opportunities to overcome the limitations of current practice through different approaches to due diligence and the creation and use of leverage.
- Better understand existing due diligence practices of Dutch banks, by contrasting facts within specific cases with current practices.

5.2 Differentiating Contribution from Linkage

Drawing on the language of the OECD Guidelines and the UNGPs, and the OHCHR Response to BankTrack, the quality of a bank's due diligence can play an important role in differentiating situations of contribution from situations of linkage – recognizing that the bank's actions or omissions should also increase the risk of the impact occurring. This includes assessing the steps taken (or not taken) in assessing impacts and in seeking to prevent or mitigate those impacts through the use of leverage.

The relevant ways in which a situation of contribution could happen are where a bank, through an action or omission, *incentivizes* or *facilitates* another party to cause harm.

- **Incentivizing** an impact generally involves a positive action or decision by a bank that has made it more likely that another party took an action or decision that caused an impact. Incentivizing implies a situation in which the other party might not have taken the action that led to the impact, but was motivated to do so by the actions of the bank.

For example, if a bank providing advisory services to a construction sector client were to urge cost-cutting measures knowing that this would pose a clear risk to workers' health and safety, without any mitigation of those risks. In this situation, the client might not otherwise have taken the cost-cutting measures in a way that would lead to a risk on workers' health and safety, but the bank has motivated the action through its advice.

- **Facilitating** an impact generally means making it possible that another party has caused an impact, by contributing to the enabling conditions needed for the impact to occur, whether by action or omission. Facilitating implies a situation in which the other party was already likely to take the action that led to the impact, and the bank's actions (or inaction) made it more likely that the other party would do so.

  For example, a bank provides financing to a mining company for country-based operations, where the government evicted indigenous peoples from their lands in order to enable the extractive activities to proceed. The government has already taken (or was already likely to take) the action of evicting the indigenous people. The bank knew about the necessary relocation of the indigenous peoples but raised no questions or concerns about the relocation plan or the impacts on indigenous peoples, as part of its due diligence (i.e., assessment and engagement around risks). The bank would not have contributed to the original impact of eviction, because it occurred before the bank had undertaken any business activities. However, as long as the impacts on livelihoods or the cultural rights of the indigenous peoples are ongoing and have not been mitigated and remediated, then the action of providing financing combined with inaction in assessing and addressing impacts on people could be seen to be contributing to the enabling conditions that allowed these impacts to continue.

- **Substantial contribution**: The OECD Guidelines further state that, for contribution through a third party to exist, a company's actions or inactions should be a 'substantial contribution', meaning 'not minor or trivial in nature'. The Working Group recognizes that further discussion is required to understand the circumstances under which a contribution would or would not be deemed 'substantial'. However, Working Group discussions highlighted that the nature of the financial product or service being provided do not, de facto, necessarily lead to or preclude situations of contribution or linkage.

Case-based discussions pointed towards an emerging framework and potential parameters for using a factor-basd approach to exploring this question.

5.3 Factor-Based Approach

In analyzing specific cases, discussions surfaced a number of factors that assisted in the analysis of whether a bank's due diligence process was adequate. This would then play a role in determining the circumstances under which omissions in the due diligence process could lead to a situation of contribution as opposed to linkage (See Box 2 below), recognizing that this is one factor among several to be considered in a full analysis of responsibility.

The discussion emphasized that these factors are enumerative rather than exhaustive, and the relevance of multiple factors in combination, rather than any single factor necessarily being itself determinative of the nature of a bank's connection to an impact. (Each factor is explored in greater depth below, supported with examples from the case scenarios the group explored).

The OECD's Due Diligence Guidance, released during the course of the Working Group's discussions, highlights three factors to help differentiate situations of contribution from linkage:

- The degree to which an activity increased the risk of an impact occurring;
- The degree of foreseeability about a specific impact;
- The degree to which an enterprises actions actually mitigated the adverse impact or decreased the risk of the impact occurring.

The Working Group recognizes that many of the factors that emerged from our discussions are related in different ways to the factors highlighted in the OECD guidance. However, the Working Group elected not to seek to align at this time the factors that emerged through its own case-based analysis with the OECD's three factors. The Working Group concluded that there could be utility in presenting the factors as they emerged, as they were specific to application of due diligence within the banking context.

Box 2

Relevant Factors Explored by the Group in Assessing Adequacy of Due Diligence

a. **Initial Knowledge:** What the financial institution knew (or reasonably should have known) about the client, country context, industry, specific risks and impacts, planned mitigation measures.
b. **Engagement on Risks:** What conversations did the financial institution have with the client and/or other stakeholders as part of its due diligence process?
c. **Transparency by Client:** If the client is a repeat client, has the client proactively discussed or brought E&S issues to the financial institution's attention? Is there a reasonable expectation that it would do so again?
d. **Incorporating Binding Expectations in Contracts:** To what extent did the financial institution communicate expectations and build leverage by including applicable E&S or human rights standards, monitoring mechanisms, and other expectations in pre-commitment and/or final (loan) agreements?
e. **Engagement After the Impact:** What steps did the financial institution take once the impact occurred, to use or build leverage to seek to influence the behavior of the client?
f. **Quality of Third Party Risk Assessment:** Where the financial institution is relying upon a third-party financial institution's risk assessment, what steps did the financial institution take to ensure it could credibly rely upon that assessment?

5.3.1 Initial Knowledge

This factor relates to what information the bank knew or reasonably should have known about the nature of the client's business, including country contexts, sector, and the likelihood of negative impacts on people. This baseline information is critical in understanding the extent to which this should have been recognized as a higher-risk relationship, and the level of due diligence process that would therefore have been appropriate.[1]

1 This factor is reflected in other approaches, such as the OECD's forthcoming 'Due Diligence Guidance for Responsible Business Conduct, in the notion of 'foreseeability'.

Specifically, the Working Group explored

1. What did the bank know, or what should it have known, about the country or countries of operations (and the level of risk for specific human rights impacts within those countries)?

   - *In case example 1, imagine that the government has a past track record of similar approaches to forcible eviction and resettlement, and marginalization of the rights of indigenous peoples. Arguably, the bank should have known the likelihood of impacts arising from the government's approach to resettling indigenous peoples in this instance.*

Case Example 1
A bank finances a mining company for its operations in country X. In order to enable the mining activity, the government evicted indigenous people from their lands through alleged intimidation and cutting off water supplies. The banks have committed to international standards on E&S performance, but performed no check on the proposed relocation of indigenous people against international standards.

2. What did the bank know, or what should it have known, about the industry sector or business activity?
   - *Again from case example 1, mining is known to be a higher-risk sector, where involuntary resettlement is a known severe impact on people if there are not proper mitigation procedures in place, and impacts on indigenous peoples should require free, prior and informed consent.*
   - *In another case example, the group explored the ship-breaking sector, where there are a limited number of country contexts where this activity takes place. Many of these country contexts are known for not having robust health and safety regulatory regimes, and the physical work is itself known to be higher-risk. A bank investing in the ship-breaking industry should become aware of these known risks.*

3. What did the bank know, or what should it have known, about the track record of the specific client in managing these risks?

   - *In case example 2, if we assume that the company has operated in this country previously, and there are active campaigns and media stories about the company alleging intimidation, termination, and violence against union organizers, the client's track record in managing these risks effectively is not strong. The bank should have factored this into their due diligence, by recognizing the client as a higher-risk relationship and requiring more robust due diligence. Failure of the bank to do this would add weight to a determination of contribution, as opposed to linkage.*

Case Example 2
A bank is involved in a bilateral lending relationship with a cement production company, where funds will be used to fund expansion of a cement project in a Central American country. There are known risks in the country related to human rights violations, particularly intimidation and violence against union organizers, including allegation of state-sponsored violence.

4. What did the bank know, or what should it have known, about the severity and likelihood of specific human rights risks or impacts connected to the client's operations?
   - *Again in case example 1, relocation of indigenous people is a known severe risk that should have been recognized and addressed by the bank.*

5. What did the bank know, or what should it have known, about any planned mitigation measures by the client to address identified actual or potential impacts?

- *From case example 3, the bank knew (and rightly should have known) about the mitigation measures planned by the company The bank therefore had reason to believe that identified risks to people would be prevented and managed effectively. This would add weight to determination that the bank could be directly linked to the impact, but not contributing to the impact.*

Case Example 3
A bank provides a bilateral loan to a company for a five-year period. Through due diligence, the bank identifies significant human rights risks facing the company, but they agree on an implementation plan with defined annual targets. After two years, it appears the company is not meeting its targets, and negative press emerges of the company's involvement in adverse human rights impacts.

- *However, in case example 1, the bank asked no questions about the mitigation measures related to resettlement. The bank's inaction or omission in this case would add weight to a determination of contribution.*

6. Members of the Working Group acknowledged that the type of financial relationship (product or service) may have bearing on expectations of what information could or should have been known to a bank in this initial phase, as part of the due diligence process. Different types of financial relationships will provide differing degrees of visibility and knowledge about a client's business activities. For example, in a project finance context, more information should be available about the specific impacts that may result from project activities, the different entities playing a role in the client's activities, and the specific mitigation measures to be undertaken. However, in a corporate lending relationship, there is likely to be less visibility up front into the full range of client activities, relationships and areas of operations. More discussion is required to explore this area, again with a view to understanding how to close the gap between current practice and what might be feasible under a strengthened approach to human rights due diligence.

5.3.2 Engagement on Risks[2]

Based on the initial knowledge of the bank and the initial assessment of the risks the bank could be connected to through this relationship, the bank could be expected to take additional steps to enhance its understanding of the risks. At a general level, if the bank did not have a sufficient amount of initial knowledge, what steps did the bank take to better inform itself of the risks?

1. What conversations did the bank have with the client about human rights risks? Did the bank seek to inform its own understanding of the risks through engagement with the client? Did the bank communicate its interest in these issues through engagement with the client?
   - *In case example 3, as part of its due diligence the bank engaged in conversations with the client company to better understand the particular human rights risks connected to the business and commit to specific mitigation measures, which would add weight towards a determination of linkage, rather than contribution.*
   - *In case example 1, even if we presume a lack of information or experience within the bank in investing in this particular sector or country context, the bank could/should have*

2 'Engagement' is used here to refer to any efforts by the bank to ask questions, seek information, or have conversations with the client. This is a broader meaning than what banks may refer to as the 'engagement' phase, distinctive from the 'assessment' phase.

engaged with the client to better inform its understanding of potential risks in this particular context. Failure to do so would add weight to a determination of contribution, rather than linkage

2. What conversations did the bank have with other stakeholders about risks related to a particular context, business activity, or company? While this type of engagement might not be expected in all cases, it would demonstrate in higher-risk projects or relationships that the bank took proactive steps to understand the risks connected to a particular client or transaction.

   - *In case example 4, where the company has denied the allegations of NGOs about severe impacts, and if we assume this is a new client relationship for the bank with no prior track record, it would be reasonable to expect the bank to engage with the NGOs to substantiate or better understand the allegations. (NOTE: The Working Group recognized that legitimate requirements of commercial confidentiality could create challenges for this type of engagement. However, several banks shared experiences of engagement with stakeholders on specific cases while anonymizing client information to protect client confidentiality).*

Case Example 4

A bank provides a line of credit / cash flow to Company A. The company is accused by NGOs of poor workplace health and safety practices, leading to toxic exposure for workers. The company denies the allegations.

5.3.3 Transparency by Client

Particularly for repeat clients, what has been the past experience of the bank in engaging with this client on E&S or human rights issues? Is it reasonable for the bank to rely upon the due diligence of the company and to trust that the company will proactively raise these issues with the bank? If so, this could potentially reduce the expectation of the level of due diligence the bank might conduct on its own as part of a new transaction.

- *In Case example 2, if we assume that the company has a track record of effectively managing this risk to trade union workers in other similarly challenging contexts, and has proactively raised this risk and its mitigation plan with the bank in this new transaction, it would be more reasonable for the bank to take this into account in determining the level of its own due diligence. This could add weight to a determination of linkage, rather than contribution.*

5.3.4 Building Opportunities for Leverage in the Relationship

In what ways did the bank signal to the client up front the importance of human rights issues, and take available steps to build leverage at the outset of the relationship?

1. Did the bank include applicable human rights standards in the pre-commitment letter or final (loan) agreement? (Or in the case of syndicate loans), did the lead bank include relevant terms, and/or did participating banks use their leverage to seek to have such provisions included? If so, this would add weight to a determination of linkage; if not, it could potentially add weight to a determination of contribution, as part of the overall analysis of responsibility.
2. Did the bank include appropriate monitoring mechanisms in the loan agreements?
   - *In case example 3, the bank included an implementation plan for mitigation actions with annual targets, and monitoring mechanisms that could help to both convey the seriousness of the bank's concern and to alert the bank when sufficient progress was not being met.*

5.3.5 Engagement After the Impact

We recognized that regardless of the quality of initial due diligence, some negative impacts could nevertheless occur or be ongoing. This could be due to the fact that initial due diligence did not identify all relevant risks and impacts. (e.g., based on an initial prioritization or de-prioritization of this particular client relationship for enhanced due diligence, circumstances evolving on the ground in the business or in the wider context, mitigation measures failing to have their intended effect, etc.). If we assume a scenario in which a past impact is directly linked to a company, companies are expected to seek to use their leverage with other parties to address the impact. For impacts that were not effectively identified or prevented, or which came to the bank's attention after the initial risk assessment process, what was the bank's response in terms of how it engaged with the client over these impacts, once they became known? Were the steps the bank took to use or build its leverage credible or effective? To what extent was remedy part of the engagement agenda?

The steps taken by the bank after the impact became known could be relevant in two different ways:

- First, in situations where an impact continues or recurs: *For example, a bank client hires a private security firm for protection of site-based assets. During an incident with community members, security personnel use excessive force, resulting in the deaths of several community members. Setting aside the question of who would need to provide or contribute to remedy for these past impacts (for which additional factors would need to be considered),* *what would be the bank's connection to future security-related incidents involving this client? The actions taken by the bank after this impact to try to ensure that the impact did not recur would bear significant weight in determining the bank's connection to future similar impacts involving this client. The bank now has additional information to inform its due diligence, and failure to take credible action to prevent this known risk would add weight to a conclusion of contribution. (Note: the bank's connection to the original impact does not change in this scenario based on engagement after the impact – but it could influence the relationship of the bank to the continuation of an ongoing impact and to future similar impacts).*

- Second, in situations where new information comes to light that might challenge the earlier assumptions on which the bank was basing its due diligence actions: *In case example 3, the bank included specific mitigation steps and a monitoring plan in the loan agreement with the company. However, if we change the facts to be that the bank instead trusted the company to determine appropriate mitigation steps itself, how would this affect the analysis of the bank's responsibility for any negative impacts that followed? The bank may have assessed the company's capacity and reasonably relied upon the company to take appropriate mitigation steps. Or the bank may not have made this assessment, and instead failed to take appropriate steps to ensure that negative impacts were prevented or mitigated. Without visibility into the bank's human rights management process and the basis for its inaction, it is difficult to determine whether failing to include specific mitigation steps in the loan agreement was appropriate. Two years later, once the impacts become known, the bank's actions to engage the client shed further light on the bank's management systems, and help with a determination of contribution or linkage as a result. The bank's connection to the past impact does not change. Rather, we may have previously lacked sufficient information on which to make an accurate assessment. There is now additional information available that changes how we might understand the bank's earlier actions.*

5.3.6 Quality of Third Party Risk Assessment

We identified several instances where a bank would likely need to rely to some extent upon the risk assessment of a third party (often another financial institution) to inform its own due diligence. For example, projects where an export credit agency may conduct initial due diligence on behalf of other lenders in a project finance context, or syndicated loan arrangements where one bank will be in the lead and conduct the risk assessment on behalf of others. This may be particularly important in the initial screening phase, where a bank is deciding what level of due diligence is appropriate for a particular relationship. In such instances, a bank relying upon the risk assessment of another financial institution could still be expected to take some steps to ensure that it can credibly rely upon that third party's risk assessment process. Some of the relevant questions a bank in such a position might ask could include (in no particular order):

1. What policy commitments does the third party have on human rights due diligence specifically (rather than generally on E&S), and is this aligned with the bank's own commitments, policies and procedures?
2. What experience does the lead bank have in arranging financing for similar projects, in similar contexts, in similar sectors? Do they have a good track record of identifying and engaging with companies or projects on human rights impacts?
3. Does the third party have experience doing its own on-the-ground due diligence, and is it doing so in this case?
4. If the third party is relying upon external consultants, what criteria does it use in hiring them? Is human rights expertise specifically required? Are they required to evaluate risks to people distinct from risks to the project or to the financial institution?
5. Has the third party financial institution searched for any supplemental sources of information?
6. What questions has the bank asked about the third party financial institution's assessment process in this case, any specific findings on risks, and what actions have been taken to mitigate these risks?
7. In a syndicated context, where client contact may be limited to the lead bank, what questions or concerns has the participating bank put to the lead bank?
8. What has been the bank's experience to date in relying upon due diligence conducted by third party financial institutions?

Case Example 5

A bank is part of a syndicate providing financing for a shipyard in an Asian country. The facility is guaranteed by an export credit agency, recognized for its expertise in this industry and the quality of its due diligence processes. Borrower is a local company who will operate the shipyard. The surrounding area is known for its artisanal fishing. At peak construction, 450 workers will be on-site, 250 of whom will come from local contractors. A local consultant conducted an environmental assessment and prepared an environmental due diligence report.

- *In Case Example 5, several relevant factors emerge regarding relying upon third parties to conduct risk assessment. The syndicated loan context likely means that the participating banks (as opposed to the lead bank) will have limited opportunity to conduct its own risk assessment and limited opportunity to engage directly with the client, creating limitations in information and time. In its own due diligence, the bank will be relying upon the risk assessment performed by others (in this case, the lead bank together with the ECA and the local consultant). The bank maintains its own responsibility to conduct due diligence, and the case raises questions about the extent to which the bank should credibly rely upon the work of others in determining what level of due diligence the bank should itself conduct.*

- In this case, the fact that the local consultant has conducted an 'environmental assessment' (rather than an 'environmental and social assessment, or a human rights assessment) should raise questions for the bank about the extent to which social and human rights issues were included in the due diligence, as well as the capacity and expertise of the local consultant to conduct those aspects of due diligence.
- This should trigger the bank to ask additional questions, channeled through the lead bank in the syndicate.
- At the same time, the fact that an ECA known for its sector-expertise and robust human rights due diligence systems is providing the guarantee should enable the bank to rely more credibly on the due diligence performed. The bank should therefore confirm through its own due diligence processes that information provided about the due diligence process and management of key risks is satisfactory.
- Working group members also highlighted the role that transparency could play, where the participating bank would explain the actions it chose to take or not take in terms of due diligence, and the rationale for doing so

(recognizing the relevance of potential constraints from regulation around client confidentiality).

5.4 Relevance of Prioritizing Higher-Risk Relationships in Corporate Lending

Working Group discussions recognized important distinctions between corporate lending and project finance, particularly in terms of the quantity of business relationships, visibility into client operations, and leverage (particularly to gather additional information).

In project finance, the number of transactions are fewer, and there are standard industry criteria for assigning a risk category to a project, based on the likelihood of certain impacts occurring (based on the IFC Performance Standards, the Equator Principles, and the OECD Common Approaches for export credit agencies). This risk categorization then determines the minimum required level of due diligence for the project (although disagreements remain about the adequacy of these frameworks and their implementation in practice)[3].

However, in corporate lending, banks may have tens of thousands of client relationships, and enhanced due diligence is not possible across each of these client relationships. Banks will therefore have to make choices early in the due diligence process about which client relationships to prioritize for enhanced focus, using the criteria of severity and likelihood of harm to people – just as businesses in other sectors may need to prioritize certain business relationships or parts of their supply chain for enhanced focus.

In practice, this means there will likely be a large number of client relationships in corporate lending that a bank may determine are lower risk, looking across the entirety of its specific portfolio. The bank might therefore reasonably and credibly not conduct enhanced assessment of risks on these relationships, instead focusing those resources on higher-risk segments of its portfolio.

The implication is that in the context of any single case of an impact occurring through a corporate lending relationship, the analysis of 'failure to act' (i.e., failure to raise questions or engage on particular risks) becomes more challenging. It

3 Several members of the Working Group highlight the opportunity to strengthen these expectations and approaches with the upcoming policy review process of the Equator Principles, and several Dutch banks are among those banks using their leverage within the banking sector to influence the Equator Principles policy review.

would be reasonable to ask the threshold question: Is this a client relationship that clearly should have been prioritized for enhanced risk assessment, given the risk profile of this specific bank's client portfolio? If not, then a failure to have conducted an in-depth risk assessment initially would likely add weight to an initial determination of linkage, and not necessarily contribution, even if impacts should occur.

The challenge in such situations is assessing whether the bank made appropriate choices in that first stage of due diligence of prioritizing higher-risk clients for more robust due diligence – using appropriate criteria and data. In such cases, additional information about the adequacy of the bank's prioritization approach, and the adequacy of bank resources dedicated to due diligence, will factor into understanding how the bank is connected to a specific impact.

The factor-based approach was also useful in assessing whether the bank made reasonable and credible choices about how to allocate its due diligence resources. These considerations could include the following:

Relevant Factors in Assessing the Credibility of a Bank's Prioritization of Client Relationships for Enhanced Due Diligence

a. Do the bank's choices reflect higher-risk relationships in practice, using the appropriate criteria of severity and likelihood of harm to people?
b. Do they reflect common knowledge about risks associated with particular industries or country contexts?
   - Is the bank utilizing available information in scalable ways to flag higher risk relationships, where possible?
   - Does the bank track and update its screening criteria and approach, based on its experience in practice and broader, evolving understandings of human rights risks?
c. Does the bank have systems in place for ongoing due diligence, which could recognize changes in circumstances or context that might elevate a particular client relationship to a higher-risk categorization and further due diligence?
d. Is the bank transparent about its process and criteria for prioritizing higher-risk client relationships (from a human rights perspective) for more focused due diligence?
e. For impacts later discovered in client relationships not flagged for enhanced assessment of risks, how did the bank engage once the impacts became known? Once additional information became available to the bank about the impact, was the bank's approach to using or increasing its leverage appropriate, given the severity of known impacts and the nature of the relationship with the client? (i.e., how can the bank's actions after-the-fact help to shed light on the quality of the bank's due diligence framework?).

5.5 Understanding Responsibility as Dynamic, Not Fixed

The Working Group explored two different approaches to understanding a business's responsibility for an impact: one that is fixed or static, and one that is dynamic. Under the dynamic approach, 'contribution' and 'linkage' are not fixed or static categories of responsibility. Rather, businesses can move from one form of responsibility to another, depending on the actions taken by the business, at different moments in time.

Authoritative institutions have now offered interpretations of the OECD Guidelines that endorse a more dynamic approach to understanding business responsibility.

- The OECD draft Due Diligence Guidance for Responsible Business Conduct state that: *'An enterprise's relationship to an adverse impact is not static. It may change, for example, as situations evolve and depending on the degree to which due diligence and steps taken to address identified risks and impacts decrease the risk of the impacts occurring.'*
- *OHCHR's Advice in Response to a Request from BankTrack states that: "a bank's involvement with an impact may shift over time, depending on its own actions and omissions.'* [4]

This dynamic approach expresses the underlying letter and intent of the OECD Guidelines and the UNGPs in seeking to incentivize good due diligence practices by companies, by recognizing that the quality of a bank's human rights due diligence practices can and should help to determine how a bank is connected to an impact.

This dynamic approach therefore requires an ongoing fact-based inquiry into specific cases, and the steps a bank has or has not taken to assess and address impacts, at different moments in time, rather than there being something inherent in the nature of certain bank products or services that would lead to an a priori determination of a particular type of responsibility. While characteristics of certain financial products may make it more challenging for a bank to conduct in depth due diligence and affect the nature of a bank's leverage, the type of product would not in and of itself lead to a particular determination of responsibility.

Working Group conversations explored what this more dynamic approach to understanding responsibility might mean in practice for banks, recognizing that additional exploration is required. Specifically:

4 OHCHR Response to BankTrack, pp 6-7.

- *If a bank has contributed to an impact through a client relationship, it could not shift to a situation of linkage solely by using its leverage in credible and effective ways after the impact has occurred. Once the bank has contributed to the impact, it can only meet its responsibility under the OECD Guidelines and the UNGPs by contributing to remedy and using its leverage to seek to influence the actions of others.*
- *However, the nature of a bank's responsibility for an impact that continues or recurs could shift over time, depending on the actions taken by the bank after the impact initially becomes known.*
- *If a bank is linked to an impact initially, the failure of the bank to exercise leverage in credible and appropriate ways could add weight to a determination that the bank (through its inaction) could shift to a situation of facilitating the continuation or recurrence of the impact.*
- *Likewise, if a bank contributes to an impact initially, contributing to remedy for the initial impact and taking credible and appropriate steps to prevent continuation or recurrence of the impact, through the use of its leverage, could add weight to a determination that the bank would be linked (rather than contributing) to future recurrences of the impact.*

The Working Group recognized two important (competing) implications from this more dynamic approach to responsibility:

- *Effective stakeholders would have less clarity and certainty about which parties are ultimately responsible for providing remedy and banks would have less clarity and certainty about potential liability;*
- *Banks would have more control in shaping how they are connected to negative impact that might occur, through appropriate due diligence steps, which incentivize good due diligence practices.*

5.6 The Role of Ring-Fencing

The Working Group understood that corporate lending to a company's headquarters operations means in most cases that the bank will be connected to the actions of a client's subsidiaries as well. With this understanding, the Working Group explored the role of 'ring-fencing', as a way to limit the scope of responsibility a bank might have for the entirety of a client's operations or business relationships. The group understand ring-fencing as providing contractual restrictions on specific client activities for which the bank's product (financing, for example) can be used and/or selectively excluding certain areas of the client's business activities. However, there were diverging views among Working Group members on how ring-fencing might factor into determining bank connection to client impacts.

- Under a ring-fencing approach, a bank would not be responsible for all the impacts a client might be connected to. Rather, a bank would only be responsible for the impacts arising from client activities connected to the bank's product or service. If the activities leading to the negative impact were excluded from the loan agreement, there would arguably be no connection between the bank's product or service and the client activities that led to the negative impact.
- Some members of the Working Group raised concerns that ring-fencing can become a formalistic escape clause for banks to shield themselves from responsibility for client-level impacts. Specific to the banking context, the fungible nature of money makes it more difficult to be sure that the bank's product is not ultimately supporting business activities that cause harm. Some members argued that the more appropriate question is whether the bank's financing makes it more likely that the client activities causing the impact will occur – whether or not that financing is tied to those specific activities.
- Others argued that ring-fencing can be one of the most powerful tools of leverage that a bank has, by signaling to companies and other banks those activities that the bank finds objectionable in a more powerful way, by including contractual language, obligations and potential penalties.

The Working Group therefore explored what a credible approach to ring-fencing might include, in order to differentiate credible efforts to build and use leverage from formalistic efforts to shield the bank from responsibility.

- Strength of contractual provisions: What additional steps is the bank taking to assure itself that the client is not using the bank's financing for proscribed purposes? What requirements is the bank placing on the client to demonstrate how it is using the finances in practice? Are there appropriate penalties in place if the client does not meet these requirements?

- Signaling heightened risk: Is the fact that the client is engaging in activities that are objectionable elsewhere in its operations, even if they are not connected to the bank's products or services, triggering 'red flags' for heightened due diligence by the bank? Does the fact that these objectionable activities continue have implications for the bank's assessment of client commitment and capacity to respecting human rights more generally?

- Complementary engagement strategy: Is the ring-fencing the only action the bank is taking to manage its responsibility, or is the ring-fencing supported by complementary engagement and additional uses of leverage around known impacts? In what ways is the bank communicating its broader expectations that its business partners to abide by the OECD Guidelines and the UNGPs.

- Heightened transparency?: Some members of the Working Group argued that the heightened risk of connection to human rights impacts in such situations should argue for heightened transparency. Others recognized the potential regulatory constraints and current industry practices around client confidentiality that could make such an expectation more challenging. It may merit further discussion to explore the extent to which banks could provide additional transparency to stakeholders about the fact that they are engaging in the relationship and the specific due diligence steps taken to prevent impacts and mitigate the risk that their financing could be used for proscribed activities?

6 Observations and Conclusions of the Working Group

The focus of the working group was to look at the role and responsibility of banks with regard to remedy, when connected to human rights impacts through client relationships. In doing so, the Working Group explored two questions:

1. How to understand the responsibility of a bank when connected to an impact through the activities of a client the bank provides financial services or products to, in terms of when the bank might have contributed to a harm, and when the bank would be directly linked to that harm. This helps define the bank's responsibility with regard to remedy.

In addressing this question, the Working Group recognized that:

- A factor-based approach provides a constructive analytical framework for assessing the nature of a bank's responsibility for impacts, and determining the bank's responsibility with regard to remedy. Through case-based discussions, the Working Group created greater alignment on the types of factors that are relevant to such an analysis.
- As a result of this factor-based approach, circumstances of both contribution and linkage are possible, when banks are connected to impacts through client relationships – and a failure to undertake adequate and effective due diligence to identify and address impacts is a relevant part of this analysis.

The working group also recognized that there is need for further discussion in several areas, across the various international forums exploring these questions, in order to:

- Better understand the role of risk categorization processes of banks within the corporate lending space, in terms of which client relationships are prioritized for enhanced due diligence approaches, in understanding a bank's connection to a specific impact.
- Understand the meaning of 'substantial contribution' in the context of the financial sector, and the roles that different factors might play in that analysis.
- Further explore the implications of a more dynamic / less static approach to understanding responsibility in the financial sector, where a bank's connection to an impact may shift over time depending on its own actions or omissions.

2. The practical roles banks could play and actions a bank could take to enable remedy in practice, across all forms of responsibility.

Through its discussions the Working Group has recognized that remedy is a relevant consideration in all cases in which a bank is connected to a negative impact, across all forms of responsibility. The WG recognized significant opportunities for banks to strengthen the focus on remedy in practice, whether in contribution or linkage situations, and thus contribute to better outcomes for people. In doing so, the Working Group found the concept of a 'remedy eco-system' to be helpful. Through this eco-system approach, the Working Group explored steps that banks can take to ensure:

- Better preparedness for remedy, by: strengthening the grievance mechanism architecture and pathways available to stakeholder should impacts occur; by targeting due diligence towards questions that position the bank and its clients effectively for remedy should impacts occur; and building leverage up front for remedy.
- Enabling remedy in specific cases, after impacts occur, by exploring the roles that banks could play and the tools they could use to play a constructive role in bringing a focus to remedy and ensuring that responsible parties meet their responsibility to provide or contribute to remedy.

According to the OECD-Guidelines and the UNGPs, businesses, including banks, have an individual responsibility with regard to remedy depending on how the business is connected to the impact. Through an eco-system approach, banks can exercise their individual responsibility to address impacts they are connected to, whether, that be through contributing directly to remedy or using leverage with other parties to seek to enable remedy in practice.

Acknowledging the practical and actual limitations that might influence the banks decision making, the working group has come up with several actions that banks could take in different stages of their due diligence. The Working Group recognizes a need to further explore this menu of actions and notes that it ultimately remains the responsibility of each individual bank to take the steps it finds most appropriate in a specific situation.

Annexes

Composition of the Working Group

During the dialogue, the Working Group used relevant Principles, Guidelines and/or other publications on the topic and spoke to various stakeholders, among others the OECD secretariat of the Working Party on Responsible Business Conduct in the financial sector.

The Working Group included:

- The representatives from the parties to the agreement and adhering Dutch banks:
  - ABN AMRO
  - Rabobank
  - NIBC
  - FMO
  - NVB
  - FNV
  - PAX
  - Amnesty International Netherlands
  - Ministry of Foreign Affairs
  - Ministry of Finance (including participation of the respresentatives of Atradius Dutch State Business)

- External experts:
  - Rachel Davis (SHIFT)
  - David Kovick (SHIFT)
  - Jeroen de Zeeuw (Timu Development)
  - Jonathan Kaufman (Advocates for Community Alternatives)
  - Joseph Wilde-Ramsing (SOMO)
  - Mariette van Huijstee (SOMO)
  - Luc Zandvliet (Triple R Alliance)

Assessing operational-level grievance mechanisms

Diagnostic questions [for the financial sector] to determine the effectiveness of [client's] GMs

During the Working Group discussions, several diagnostic questions were discussed, based on previous work from Shift and Triple R Alliance. This Annex provides an overview of relevant questions that can help assess the effectiveness of existing Grievance Mechanisms (GM).

Questions that Banks can ask with regard to measuring the effectivess of the design process of a Grievance Mechanism

Question	Comments/Evidence
Did the perspectives of affected stakeholders inform the design of the grievance mechanism?	Evidence of any consultation processes or other venue where stakeholders could provide input
Are user representatives involved in the oversight of the grievance mechanism?	e.g. as part of a second order mechanism involving community reps or as an oversight committee or worker/management committee
Are there clear and predictable processes for how grievances or complaints get addressed?	Evidence of a grievance procedure
Are contractors contractually required to follow the company grievance procedure	Evidence of the standard contracting clause re: grievance management
Has the company a mechanism to deal with the concern of retaliation?	Evidence that anonymous grievances are lodged as well as have been managed effectively The procedure discusses how the company will deal with the risk of retaliation
Are complainants able to be accompanied in the grievance process by a worker representative, an advocate, or other forms of support?	Evidence of communication materials where this is explicitly mentioned
Does the grievance mechanism have an credible and impartial appeal mechanism	Evidence that (some) grievance investigation outcomes change after being appealed
Has the General Manager signed off on the grievance mechanism?	Evidence of the signatory page of the procedure
Do all complaints receive a response from management, either indicating what action was or will be taken or the reasons no further action was taken?	Evidence of examples of signed close out forms
Is there management accountability for the grievance mechanism?	Evidence that senior manager been designated as responsible for responding to complaints Evidence that effectiveness of a GM is linked to a bonus system
Does the company publicly report how it has adapted its approach as a result of grievances	Evidence of communication to this effect

Questions that Banks can ask with regard to measuring the effectivess of the implementation of the Grievance Mechanism

Question	Comments/Evidence
% cases (not) acknowledged within agreed timeframe	The grievance register Monthly report
Trends in percentage true/false claims	You would want to see a downward trend
# of complaints that remain unresolved for more than 3 months after they were logged	The grievance register. Grievances staying open for > 3months need to have a justification
How does the company know if affected stakeholders (i.e., users and intended users) are satisfied with the process and/or the outcomes?	% of cases close out 'negatively' for outcome but 'positively' for process
How does the company know if the grievance mechanism is working in practice?	Evidence of perception survey's Evidence that the same users are using the grievance mechanism again

Questions that Banks can ask with regard to measuring the effectivess of the overall social performance approach of the company

Question	Comments/Evidence
What % of assets have a GM that is aligned with the UNGPs?	Evidence of an internal audit that identified the presence of a grievance procedure
Are there any Repeat grievances?	Evidence that companies track repeat grievances
What are the trends in specific human rights related complaints?	The nature or 'seriousness' of grievances needs to decrease over time (evidences in the grievance register)
Numbers of grievances per theme and/or departmentment/contractor	These indicators should be reviewed against the project phase and if there is a justification for certain patterns

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