

Fit for Purpose? An Analysis of Development Finance Institutions' Management of Human Rights Risks in Intermediated Finance

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ABOUT THIS COMPANION

This companion brief brings together in one consolidated overview the sections in the [Fit for Purpose report](#) discussing the implications of the UN Guiding Principles on Business and Human Rights (UNGPs) for development finance institutions (DFIs) in respect to their management of environmental & social (E&S) risks in intermediated finance.

The overview below zooms in on important elements of the UNGPs that relate to the human rights concerns and gaps identified and discussed in depth in the Fit for Purpose report. **It is intended as a quick reference guide for the DFIs seeking to understand how to draw upon international business and human rights standards to strengthen their E&S policies and procedures (referred to as Safeguards) for financial intermediaries (FIs) clients and transactions.**

The resource can be used by DFI staff, the management of DFIs, DFI shareholders as well as their external stakeholders. Those seeking a comprehensive analysis of key human rights concerns in respect to the DFIs' Safeguards for intermediated finance and granular recommendations for a more robust DFI E&S risk management system for intermediated finance should consult the Fit for Purpose report.

BACKGROUND

The [United Nations Guiding Principles on Business and Human Rights](#) (UNGPs) are the authoritative normative standard on the duty of states to protect against business-related human rights abuses and the responsibility of business enterprises, including financial institutions, to respect human rights. The UNGPs establish the baseline expectation that all businesses – including development finance institutions – irrespective of size, sector, operational context, ownership, and structure, should respect human rights in their own activities and value chain.

The UNGPs have been reflected in other standards – commonly referred to as “business and human rights” or “responsible business conduct” standards – notably the [OECD Guidelines for Multinational Enterprises](#). Since 2011, numerous authoritative interpretations issued by the UN Office of the High Commissioner for Human Rights (OHCHR) and the Organization for Economic Cooperation and Development (OECD)¹ have clarified the human rights responsibility of financial institutions. Of particular interest to DFIs are the OECD [Guide on implementation of Responsible Business Conduct Due Diligence in the context of project finance](#) (2022) and OHCHR's [Benchmarking Study of Development Finance Institutions' Safeguard Policies](#) (2023).

¹ See OHCHR, [Business & Human Rights](#) webpage, [Financial Sector resources](#); the OECD, through a collaborative, multistakeholder approach involving states, financial institutions and CSOs, published guidance documents that operationalise human rights due diligence for institutional investment, corporate lending, securities underwriting, and project and asset finance transactions: see OECD, [Responsible Conduct in the financial sector](#).

The Fit for Purpose report and this Companion aim to complement these analyses by focusing on gap areas in the DFIs' E&S risk management for intermediated finance as compared with the UNGPs, and by advancing recommendations to close the respective gaps.

STRUCTURE OF THE COMPANION

The UNGPs and OECD Guidelines set out a three-part framework for building respect for human rights by businesses, including financial institutions such as DFIs, into everyday operations. Specifically, businesses are expected to: adopt a policy commitment to respect human rights; implement an ongoing human rights due diligence (HRDD) process; and have procedures in place to provide and enable remedy in case negative impacts materialise.²

These three components frame the analysis in the table below which includes:

- A brief overview of expectations under the UNGPs
- A list of attention points or recommendations about how these UNGPs expectations can be translated by DFIs into policy and practice
- References to relevant sections in the Fit for Purpose report for more background and analysis.

² See OHCHR, [Interpretive Guide to the corporate responsibility to respect human rights](#) (2012).

POLICY COMMITMENT TO RESPECT HUMAN RIGHTS

The UNGPs and the OECD Guidelines set the expectation that businesses, including DFIs, should adopt policies to express their commitment to respect human rights. These policy commitments should steer the approach of businesses to identifying and addressing negative human rights impacts of their activities. The UNGPs incorporate within the scope of business responsibility all interrelated business relationships – relationships in value chains (both upstream and downstream), as well as the customers to which a business provides its own goods or services. There is no exclusion of the financial sector or certain financial relationships from the scope of responsibility.

Relevant sections in Fit for Purpose report: [sections 4](#) and [7.3](#).

UNGPs Elements on Policy Commitments	Implications for the Scope of Application of DFIs' Safeguards for Financial Intermediaries (FIs)
<ul style="list-style-type: none"> ✓ No limitation of the scope of application to the financial sector: The UNGPs apply to financial institutions, their financial relationships, clients, and financial value chains. ✓ Scope and reach of business responsibility: Covers the entire financing value chain. 	<ul style="list-style-type: none"> → DFI Safeguards should apply to financing through FIs, including all types of FIs across the entire portfolio, and to the entire FI value chain, including sub-sub-projects. → No type of financial transaction should be excluded from DFI Safeguards, risk management or assessment of potential E&S risks and impacts, including human rights, and the DFI's link to them per se. The DFI should take a risk-based approach – meaning that while there can be graduated approaches with more specific requirements for higher risk projects or transactions, the approach should be grounded in a human rights risk-based analysis and should not exempt whole categories of financial transactions without considering risks.
<ul style="list-style-type: none"> ✓ Scope of human rights coverage: Policy should cover all human rights. 	<ul style="list-style-type: none"> → DFI Safeguards should cover the full range of human rights, noting that existing Safeguards typically cover a limited range of human rights (and at times a limited scope of those rights) such as labour rights, Indigenous Peoples' rights, etc.
<ul style="list-style-type: none"> ✓ Specificity: Policy should be specific to the actual activities and value chain. 	<ul style="list-style-type: none"> → DFI Safeguards should address and be adapted to all forms of FIs and FI transactions (e.g. including trade finance, capital market transactions, microfinance).
<ul style="list-style-type: none"> ✓ Clarity: Policy should set clear expectations on actions and behaviour by DFI personnel, FIs, and sub-clients in their value chain. 	<ul style="list-style-type: none"> → DFIs should provide clarity in their Safeguards on the principles for and application of their Safeguards to different types of FI transactions and the respective roles and responsibilities of DFIs, FIs and sub-clients.

HUMAN RIGHTS DUE DILIGENCE (HRDD)

The UNGPs and the OECD Guidelines set out a risk-based approach to due diligence to identify, prevent, mitigate, and account for risks and negative impacts on human rights. It is similar to the DFI Safeguards approach in that it prompts DFIs and their clients to look at the risks and impacts of operations on people rather than impacts on the DFI or FI itself. The UNGPs make it clear that risks to people is the primary element of risk management rather than one factor amongst many, which still characterize some of DFIs' approaches.

Relevant sections in Fit for Purpose report: [sections 5](#) and [7.3](#).

UNGPs Elements on HRDD	Implications for DFIs' E&S Risk Management System for FI Financing
<p>✓ Embedding: HRDD processes should be embedded into management systems, processes, and oversight bodies.</p>	<p>→ DFIs already require FI clients to put in place organisational capacity and competency to oversee their environmental and social management systems (ESMS). An HRDD approach would encourage more systematic DFI support for and oversight of FI clients to implement these systems appropriately in relation to human rights risks.</p>
<p>✓ Focus: HRDD focuses on processes and outcomes.</p>	<p>→ DFIs' appraisal and supervision should focus not only on the existence of an ESMS and related procedures but also on the actual outcomes such ESMS is leading to – in other words, is the ESMS effective at preventing, mitigating, and remediating human rights risks and impacts? And how does the FI adapt the ESMS in response to gaps identified?</p>
<p>✓ Assessment followed by prioritisation where necessary: HRDD processes require an assessment of risks and impacts on people followed, where necessary, by a prioritisation process to prioritise the most severe risks based on the scale, scope and irremediability of such risks.</p> <p>✓ The scale and complexity of a DFI's HRDD processes and tools should depend on the size of the FI, the nature and context of its operations and the severity of its potential adverse human rights impacts across its portfolios.</p>	<p>→ Prioritisation of risk management measures is needed in a DFI context given DFIs' extensive portfolios of FI clients. However, that prioritisation should have as starting point an assessment of the severity of risks for people and the environment in the specific transactions rather than excluding whole types of transactions/funding models from assessment based solely on the type of transaction.</p> <p>→ DFI sub-projects and sub-transactions that present higher risks for people and their human rights should be prioritised for appraisal and supervision.</p>

<p>✓ Distinct Responsibilities: All businesses in a value chain have distinct responsibilities to prevent and address human rights impacts. The UNGPs do not intend to shift the burden of responsibility for the impact from the business enterprise causing the impact, but instead highlight the different responses required from each business partner depending on their type of “involvement” with the adverse human rights impact.³</p>	<p>→ In complex business relationships such as those entailed in FI scenarios, the DFI’s responsibility to respect human rights cannot be discharged by transferring or delegating responsibility to FIs. Instead, the expectation is that each business (i.e. DFI, FI and sub-client) discharges their responsibility according to how they are “involved with” the adverse human rights impact in UNGP terms (e.g. depending on if they “caused,” “contributed” to or are “directly linked” to the adverse impact). Thus, collaboration between the DFI and FI should be expected rather than full delegation of all responsibilities to the FI.</p> <p>→ DFIs should ensure that FIs prompt their clients to respect human rights and carry out HRDD.</p>
<p>✓ Iterative, not one off: HRDD is a dynamic process rather than a one-off process so that risks and impacts are assessed periodically and as needed.</p>	<p>→ DFIs’ monitoring/supervision should include a) regularly assessing whether the FI’s ESMS is adequate and proportionate to the changing risks in the FI’s portfolios and b) responding to incidents and reports of human rights impacts among FIs’ clients.</p> <p>→ DFIs should ensure that FIs are regularly monitoring the effectiveness of their ESMS and updating it to be able to identify and capture new risks in their portfolio and activities.</p>
<p>✓ Stakeholder engagement is a central element of HRDD and enables businesses to assess their human rights risks and impacts accurately in a manner informed by the views of those potentially and actually affected.</p>	<p>→ DFIs should a) require FIs to a conduct engagement with affected stakeholders and/or their representatives in relation to the development and implementation of the ESMS and in relation to high-risk projects and b) require higher risk sub-clients to conduct stakeholder engagement too.</p>

³ The UNGPs introduce a framework to differentiate between different types of business involvement with potential adverse impacts. According to this framework, a business can “cause”, “contribute to” or “be directly linked” to an adverse impact. Different actions to address adverse impacts are envisioned depending on the type of involvement. For an overview of this framework and guidance on its application to the financial sector see e.g. OECD, [Responsible Business Conduct Due Diligence for Project and Asset Finance Transactions](#) (2022), pp. 31-34. For a practical resource on identifying the three types of involvement, see Legacy Landscapes Fund, [Guidance Note: Environmental and Social Action Plan Development](#) (inc. UNGPs implementation), section 5.1. (2023).

RESPONSIBILITY FOR REMEDY

International human rights law sets out the basic principle that if someone's human rights have been harmed, they should have access to remedy that can redress the harms. That includes an appropriate process to address the harm and appropriate actions to redress the harms. The UNGPs and the OECD Guidelines provide a widely accepted framework for assessing the remedial responsibilities of DFIs and their FI clients, considering their respective involvement in negative human rights impacts. Engagement of affected stakeholders is a core part of the process and is underpinned by disclosure of information.

Relevant section in Fit for Purpose report: [sections 6 and 7.3](#).

UNGP Elements on Remedy	Implications for DFIs' Accountability and Remedy System for FI financing
<p>✓ Appropriate action in response to harms requires: (i) Use of leverage to enable actions to remediate harms if the business, including financial institution, is "directly linked" to harm through e.g. its financing; (ii) Action to remedy harm if the business, including financial institution, has "caused" or "contributed" to harm through e.g. its financing.</p>	<p>→ DFIs will often be "directly linked" to adverse human rights risks and impacts through their FI financing, in which case they should use their leverage with their FI clients to prompt the FI to address and remedy the problem with their sub-clients. This is already in principle part of DFI practice at most but not all DFIs. Thus, while this may require renewed attention with FI clients on the importance of addressing harms, it is not a new practice.</p> <p>→ If the DFI is "contributing" to the harm by incentivising or facilitating the harm through its own actions or omissions alongside the FI or at the sub-project level, the DFI, alongside the FI and/or sub-client, would be expected to contribute to remedy in some way.</p>
<p>✓ Grievance mechanisms to deal with harms: Businesses should establish operational level grievance mechanisms so they are prepared to respond effectively to grievances if they do arise, in line with the UNGPs' "effectiveness criteria."⁴</p>	<p>→ DFIs should establish Independent Accountability Mechanisms (IAMs), drawing on established good practices.⁵ IAMs structures and processes should be designed to reflect the UNGPs' effectiveness criteria for grievance mechanisms.</p> <p>→ IAMs should have a mandate to accept FI-related complaints.</p> <p>→ DFIs should require FIs and sub-clients to establish operational grievance mechanisms in line with the UNGPs' effectiveness criteria.</p>
<p>✓ Consulting with and involving those harmed in deciding on remedial action is considered a core requirement in addressing grievances.</p>	<p>→ Where grievances have been brought to IAMs or DFIs about FI-related negative impacts, IAMs and DFIs should engage with affected communities to understand the grievances.</p> <p>→ DFIs should consider providing support, advice and/or technical assistance to their FI clients in handling more serious grievances.</p>

⁴ OHCHR, [Remedy in Development Finance: Guidance and Practice](#) (2022), Annex II.

⁵ Accountability Counsel et al, [Good Policy Paper: Guiding Practice from the Policies of Independent Accountability Mechanisms](#) (2024).