

# ESG Viewpoint

June 2017

## Securing human rights in extractives industries

> **Goal:** Improve management of human rights risks in extractives industries

> **Engagement since:** 2015

> **Sectors involved:** Metals & Mining, Oil & Gas

### Juan Salazar

Associate Director  
Governance and Sustainable Investment

### Matthias Beer

Associate Director  
Governance and Sustainable Investment

## Contact Us

### Institutional business

-  +44 (0)20 7011 4444
-  institutional.enquiries@bmogam.com
-  bmogam.com/responsible-investing

### Discretionary Sales

-  +44 (0)20 7011 4444
-  client.service@bmogam.com
-  bmogam.com

### UK Adviser Sales

-  0800 085 0383
-  sales.support@bmogam.com
-  bmogam.com

### Key summary

- BMO Global Asset Management joined an investor collaborative initiative to engage with 50 companies in the extractives industries to drive stronger human rights risk management practices to enhance value creation.
- Companies listed in developed markets are generally more advanced in how they understand and manage human rights issues than their peers in emerging markets
- Biggest areas for improvement are disclosure of human rights practices and performance in the case of leading companies, and embedding human rights commitments into corporate practice in the case of laggards

### Background

The oil, mining and gas industries are essential to the economies of many developing countries. At the same time, mineral and energy developments profoundly transform environments, communities and economies – and can often generate social conflict. There is increasing evidence that violations of human rights, or even perceived violations of human rights, can be causes, consequences and potentially forecasters of social unrest and conflict.

Costs to extractives companies from social unrest or conflict can significantly impact their ability to meet production and sales forecasts and hence deliver sustainable growth. Costs usually arise from lost productivity due to temporary shutdowns or delays; or staff, including senior management, being diverted to managing conflict. Furthermore, companies involved in social conflict can bear opportunity costs in terms of the lost value linked to future projects or expansion plans that did not materialise.

Poorly managed human rights risks can therefore pose a significant source of operational, legal and reputational risk to companies and, ultimately, affect their ability to retain their social license to operate and deliver growth.

The launch of the United Nations Guiding Principles for Business and Human Rights (“the Guiding Principles”) in 2011 marked a major turning point as they signaled broad-based acceptance of the fundamental principle that business should be responsible for actively managing the risks of human rights abuses linked to their activities. As a result, expectations of business with respect to human rights became much clearer.

### Engagement action

Recognising this, and aiming to address risks to our clients’ portfolios, BMO GAM joined in 2015 a two-year collaborative engagement initiative facilitated by the Principles for Responsible Investment (PRI). Using the Guiding Principles as a key reference point, the initiative identified six areas for engagement, including human rights commitment, embedding it into corporate practice, human rights due diligence, and grievance mechanisms.

Investors contributed to selecting a list of 50 large global extractive companies considered to be particularly exposed to human rights risks. The list included companies such as **Glencore, Anglo American, Southern Copper, BHP Billiton, PetroChina, ExxonMobil, Total, and Royal Dutch Shell**. We led engagement on behalf of the group with three companies, and closely supported dialogue with an additional five.

### Key findings

Engagement revealed that human rights related issues receive management attention across all companies in the list, albeit to varying degrees. With only a few exceptions, all companies have a human rights commitment. This can be in the form of a standalone policy or incorporated into other documents, e.g. sustainable development/corporate social responsibility policy, code of ethics. Differences in company practices and the level of management attention became clearly evident beyond those initial commitments.

Companies domiciled in Europe and North America are, unsurprisingly, more advanced than their peers in emerging markets in their approach to managing human rights risks by:

- Having board oversight and management accountability mechanisms, and taking steps to embed human rights into existing risk management systems and budget planning processes;
- Developing consistent approaches to human rights due diligence as evidenced by ongoing risk management processes to identify, mitigate and account for how they address their adverse human rights impacts;
- Implementing robust stakeholder engagement and consultation practices aimed at building sustainable relationships with local communities;

- Tackling challenges linked to setting up accessible and effective grievance mechanisms; and
- Taking a strategic approach to community investment.

The main areas for which we identified need for improvement were grievance management, transparency and disclosure, as well as linking human rights performance to executive pay. In particular, companies should work on improving the extent to which existing grievance mechanisms effectively capture information about social risks, including human rights risks, and on providing material and meaningful information about their human rights processes and performance.

Companies based in emerging markets generally failed to demonstrate sufficient recognition of the risks to the sustainability of their businesses from poor management of issues related to human rights, particularly those concerning communities directly affected by their extractive activities. This despite mounting evidence pointing to the contrary. For example, battles over the exploitation of natural resources have become common throughout Latin America. The Observatory of Mining Conflicts in Latin America, a coalition of NGOs, logged 215 of them in 19 countries in 2014, led by Mexico, Peru and Chile.

We encountered a number of cultural and contextual barriers that prevent companies from fully understanding and addressing human rights risks and, ultimately, the potential costs to their businesses. These include: narrowing the attention of human rights management to labor rights only, instead of all potentially affected stakeholders; resisting engagement with local communities to understand and manage expectations; misconceiving that local communities are powerless in the face of large corporations and governments; and limiting transparency and accountability in the governance of countries’ natural resources.

### Conclusions and next steps

This collaborative engagement effort revealed that despite companies’ policy commitments to respect human rights, many continue to struggle with supporting the effective implementation of such commitments. This is particularly the case for those companies based in and operating in emerging markets.

Faced with increasing pressure from civil society, governments and investors and other financial actors, companies will have no choice but to act. Guidelines such as the UN Guiding Principles and the OECD Guidelines for Multinational Enterprises have become de-facto standards for defining corporate responsibility for human rights. This effectively means that the kinds of policies and processes

that extractive companies need to put in place to prevent and address negative social and human rights impacts and their associated costs are clear and increasingly well understood.

Companies like Anglo American, BHP Billiton and **Rio Tinto** increasingly understand the connections between key systems – for identifying human rights impacts, responding to grievances, and tracking performance – and are taking steps to refine them to better manage their risks and mitigate their impacts. Moreover, they have highlighted the benefits of operating in partnership with communities to achieve mutual value creation.

We firmly believe in the importance of robust approaches to human rights risk management for sustainable value creation. By preventing negative human rights impacts and maximising positive ones, extractives companies will reduce operational costs, improve stakeholder relations, and secure their social license to operate. Therefore, we will continue engaging with both leading and lagging companies to help drive stronger practices across the extractives industries.

#### The Corporate Human Rights Benchmark (CHRB)

With extractive companies still struggling to disclose material and meaningful information on their human rights practices and performance, we welcomed the launch of the results of the Corporate Human Rights Benchmark (CHRB) initiative earlier this year. The CHRB's objective is to rank companies across the extractives, apparel and agricultural products industries on human rights performance based on publicly available information. We are somewhat concerned about the risks of implying human rights performance can be determined solely by what companies report in their public documentation. However, and given the competitive nature of the market alongside the increasing significance and commercial relevance of effectively managing human rights, we fully recognise the role the CHRB can play in driving change.

#### Investment Week Sustainable Investment Awards

Best Ethical Investment Fund Management Group 2016



Best Sustainable Investment Fund Management Group 2016



Outstanding Contribution 2014



Fair Pensions 2014



The information, opinions, estimates or forecasts contained in this document were obtained from sources reasonably believed to be reliable and are subject to change at any time.

© 2017 BMO Global Asset Management. All rights reserved. BMO Global Asset Management is a trading name of F&C Management Limited, which is authorised and regulated in the United Kingdom by the Financial Conduct Authority. UK, AT, BE, DK, FI, FR, DE, IE, IT, LU, NL, NO, PT, ES, SE. FRN:119230. CM13336 (06/17)