

Statement on

The Shift-Mazars Discussion Paper on “Developing Global Standards for the Reporting and Assurance of Company Alignment with the UN Guiding Principles on Business and Human Rights”

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Introduction

The Shift-Mazars discussion paper sets forth a project to develop international standards that companies can use to report on human rights as well as standards for the “independent assurance” of these reports. The proposal is for Shift, a non-profit consultancy in the area of human rights, and Mazars, an international company providing auditing, accountancy and advisory services, to develop these standards using consultations and through pilot projects.

This project is based on misunderstandings about standard setting, misunderstandings about issues and initiatives related to non-financial reporting and misunderstandings about contemporary assurance and social auditing practices. The proposal seems more about accommodating the Guiding Principles to existing CSR practices and the interests of the CSR industry than using the Guiding Principles as the basis for reconsidering and reshaping the expectations of what constitutes responsible business behaviour. This project is not what is needed at this time to give effect to the Guiding Principles and will likely interfere with the broader and deeper discourse that needs to take place on subjects such as due diligence and remedy. These are fundamental flaws that make it likely that this project will do more harm than good.

Standard setting

This project does not constitute a legitimate basis for standard setting and, hence, any product can be credibly challenged. Setting credible standards requires a transparent and rule-based process which includes the participation of all of the right parties. The process must have a governance system designed to achieve a high level of consensus among all of the necessary parties. The paper does not propose any such process and is oblivious to its essential nature. It would be fair to infer that decisions are to be made by Shift and Mazars. These organisations are not the right parties to either set these standards or the rules for developing them.

This project is reminiscent of CSR initiatives developed by a small group that were “road tested” and then recommended to companies as “best practice”. While some of these initiatives were of value, they did not result in anything accepted as a standard. This kind of process is not a legitimate way of setting a reporting standard that may come to have legal implications or for a standard that would be used by enterprises to sell services that are directed at the public trust and to influence public policy.

The right parties are not involved. Setting technical standards requires the participation of experts. Standards involving public policy require the participation of representatives. (The ILO sets public policy standards for labour issues based on the participation of governments and the most representative organisations of workers and employers.) The proposal does not provide for either the range of expertise required or representatives of the interests that should be taken into account.

Financial reporting is related to non-financial reporting only by analogy. The expertise and experience of accountants is not completely applicable to this kind of non-financial reporting. Our experience, which includes a long involvement with the Global Reporting Initiative and with ESG disclosures intended for fund managers and pension fund trustees, is that much of what is advanced by accountants for reporting on the social impacts of business activities is inappropriate. This would include the promotion of quantifiable indicators in the social area that are not valid measures as well as arguing for inappropriate reporting boundaries and materiality tests. The involvement of an auditing and accounting enterprise in this project is based on the idea that the accounting industry possesses the expertise needed for setting non-financial reporting standards or to create a market-creating standard for assurance providers. This is not true.

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Non-Financial Reporting

This proposal does not take into account relevant initiatives and issues related to non-financial reporting. The proposed standards would not be filling a vacuum. The Global Reporting Initiative established a Working Group on Human Rights which resulted in changes for human rights reporting to its *Sustainability Reporting Guidelines* in 2011. The new G-4 version of the *GRI Guidelines*, released this May, contains even more changes intended to bring sustainability reporting more in line with the Guiding Principles, notably in the areas of reporting boundaries, the Disclosure of Management approach narrative for describing due diligence, materiality based on impact and on business relationships in the supply chains. Although the GRI Guidelines are not perfect, they are widely recognised and used. They are sufficient for the time being. Additional reporting guidelines may be needed – but after there is greater understanding and agreement over what constitutes due diligence in specific situations.

The proposal overlooks the issues arising from non-financial reporting that are controversial or that result from obfuscation. The conflation of the sustainability of an enterprise that is of interest to investors on one hand, with sustainable development which is the broader societal interest on the other hand, is such an obfuscation. It is also germane as one important contribution of the Guiding Principles was to shift the focus away from the business enterprise and to focus instead on rights-holders and the societal interest.

In this respect it is important to consider the term “risk”. Due partly to the importance given to the “business case” by CSR advocates, “risk” is almost always understood to mean “risk” to a business enterprise in obtaining its objectives and not as “risk” to those that may be adversely affected by the activities of the business enterprise. The focus must be on the rights-holders. The proposal seems somewhat reluctant to do this: “In line with the UN Principles, both the Statement and the Assurance review would consider risk not just from the perspective of the company but also from the perspective of those potentially impacted.”

Part 4 of Annex B entitled the “Integrated, Cross-Functional Decision-Making to address Human Rights Impacts” provides a telling sentence in this respect. This part begins with a summation of Principle 19 which is about what a business enterprise should do in order to prevent or mitigate adverse impacts. The principle sets forth the need for a business enterprise to integrate its impact assessments and also clarifies how appropriate action varies depending on whether it causes, contributes to or the impact is linked to it. In the list of the possible elements to be included that follows this, the first sentence may have mistakenly replaced the word “impacts” with the word “risks”: “The Company’s efforts to mitigate its human rights risks, with particular attention to its salient risks.” The term “impacts” would put the focus on those adversely affected but the term “risks” is ambiguous, and more often than not, is interpreted to be risks for the company. Neither Principle 19 nor its Commentary refers to “risks”. A reporting standard should require that the term “risk” be used in an unambiguous way.

One of the arguments for non-financial reporting is that it can be used to improve the management of the business enterprise. Management terms and concepts are important parts of sustainability/social responsibility reporting frameworks. However, not all management concepts are appropriate for human rights discourse. Consider the concept of “continuous improvement” which is usually demonstrated through metrics. While the concept could be applied to a due diligence process, it is inappropriate for comparing adverse impacts on human rights. For example, it is not acceptable to claim improvement because the number of child slaves used in one reporting period is less than the number used in the previous reporting period. Any child slavery is always unacceptable. The proposal does not seem sensitive to this problem where it suggests that expectations focus on continuous improvement. Note that in promoting continuous improvement, the proposal refers to “challenges” instead of “adverse impacts”.

The belief that “what cannot be measured cannot be managed” has led to the use of a lot of spurious quantifiable indicators in sustainability/ social responsibility reports. This has been particularly true in the labour and human rights sections of these reports where figures concerning the “number of violations” or

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the “number of hours of training” are typical. It is unreasonable to expect a business enterprise to report on adverse impacts especially where they are also illegal. However, even process issues are not easily quantified. A narrative explanation in plain language of a due diligence process would be better.

A controversial issue in non-financial reporting is materiality. The practice of determining materiality on the basis of the needs of likely report readers is not a good idea in this case. The problem is that deciding what to report on is another way of deciding what is important. The danger is that the responsibilities of business with respect to human rights set out in the Guiding Principles could be effectively redefined by widespread reporting tailored for investors. In the end materiality for human rights reporting must be based on an interpretation of the internationally agreed human rights - and that should not be made by the assurance provider.

Our experience is that sustainability/social responsibility reports do not adequately report on labour practices or how the company impacts the human rights of workers. Yet the human rights of workers would reasonably be among the most salient human rights for almost all business enterprises.

The problem of assurance

This proposal gives too much influence to the accountancy profession and to assurance providers both in standard setting and ultimately as arbitrators of business responsibility for human rights. The project is at least premature and does not address urgent needs. It will, however, interfere with other work that is more important.

The rise of non-financial reporting has resulted in a new industry of enterprises that provide services to companies on preparing their reports or that sell “assurance” of reports. The financial accounting/auditing industry has become involved in both of these activities. However, the selling of “assurance” for non-financial reports is the more problematic activity. Indeed the value of assurance of these reports and the nature of the enterprises that provide this assurance is controversial.

Although the accountancy profession has adopted a standard for assurance engagements for non-financial information, it is inadequate for this work. There is far too much scope for interpretation and for so-called “professional judgement” and insufficient provision for stakeholder engagement. As with financial reporting, materiality is determined by the needs of the intended users of reports which are not a good test for human rights reporting. The standard was developed to provide a means for financial accounting/auditing enterprises to sell assurance for sustainability/ social responsibility reports. There is also another standard developed independently but with fewer users. Although the accountancy profession has claimed this activity to fall within its competency, this has not been accepted by many of the stakeholders having an interest in corporate transparency and accountability.

In practice, the scope of what is assured in sustainability/ social responsibility reports is not large and can be limited to the processes used in preparing the report or to data verification. This in itself can be misleading. The selling of assurance for non-financial reports may not be sufficiently regulated. The attestations of assurance providers go unchallenged. We are not aware of any sanctions either professional or legal. Unless legally required to do so, it is difficult to see how any business enterprise would publish a letter from an assurance provider that declared that there were omissions and misstatements. The accountancy profession’s model for self-regulation and ethics may not be the right model in this environment. The independence of assurance providers from the companies that engage their services should not be seen as a settled question

We have reasons to question the competency of assurance providers. One reason is the number of assured reports that omit information about labour practices and human rights that should be considered material. Moreover, many civil society organisations that demand that sustainability/ social

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responsibility reports be verified do not consider commercial assurance providers to be the solution. The proposal declares the competence and independence of assurance providers to be crucial, and includes suggestions for competences, but it does not recognise these problems.

The discussion of assurance on Page 8 relates widely shared critiques of social auditing and certification of supply chain labour practices to critiques of sustainability/ social responsibility reports that “are not subject to appropriate external assurance”. It is difficult to understand how the challenges to the credibility of social auditing and to certification of workplaces can be used to promote the certification of human rights reports. Instead, the experiences with CSR initiatives addressing labour practices provide good reasons to question the kind of certification that assurance providers can offer for human rights. Yet the proposal is for assurance providers to “assess the existence, suitability and effectiveness of policies and processes that make up the company’s human rights management system.” It would be difficult for us to accept that assurance providers could or should validate claims about working conditions or labour practices. This is another reason why other expertise and interests need to be included in the governance of this project.

A serious concern is that assurance providers will be given a role as arbitrators of CSR initiatives and already established standards – with the effect of undercutting or of conferring legitimacy on various initiatives. The greatest danger is that assurance will become an obstacle to victims and human rights defenders who will first have to discredit the assurance provider before effective pressure can be put on the business enterprise that has caused harm. This must not become the protection that will motivate business enterprises to purchase letters of attestation for their reports.

What is needed now

The *UN Guiding Principles for Business and Human Rights* are a new way of thinking about business responsibility and a set of expectations as to what constitutes responsible behaviour. They provide an important corrective to many of the worst ideas associated with the Corporate Social Responsibility phenomenon. For the *Guiding Principles*, responsibility is not a “voluntary concept” and respecting human rights is not “optional”. The roles of the state and of business enterprises are distinct and independent. Unlike the CSR world, where the focus is on positive contributions that business enterprises may choose to make, the *Guiding Principles* focus is on adverse impacts that business enterprises must address. There are, of course, other important ideas in the *Guiding Principles*. The point is that the *Guiding Principles* are a conceptual framework that can be used to guide both public policy and private behaviour.

The *Guiding Principles* are not, however, an auditable standard. They address behaviour with relation to the entire scope of internationally recognised human rights as set forth in various international instruments. This project is premature because there needs to be considerably greater understanding of at least two aspects of the *Guiding Principles*.

The *Guiding Principles* establish due diligence as the expectation of responsible behaviour in this area. They do not provide the answer as to what due diligence would mean in specific situations or with respect to specific human rights. The “due” in due diligence means that the process must be commensurate with the risk to rights holders and the severity of adverse impacts on their human rights. This process cannot be reduced to a universal checklist. While performance indicators can be verified, they are not likely to be useful.

The other aspect is remedy. There is no commonly held understanding of what would constitute remedy in various situations. The *Guiding Principles* provide less guidance than they do about due diligence.

Enterprises seeking to sell accounting and auditing services have little to offer by way of increasing our understanding of these aspects. Yet the effect of this project would be to give them a privileged position in an important public policy debate that needs to take place.

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Companies have much to do by way of applying the Guiding Principles in their daily operations and there is much to learn. Subcontracting responsibility to the CSR industry will likely undermine the progress that has been made and transform what should have been a fresh approach into business as usual.