

Human Rights in Your Supply Chain Isn't Just Good Business — Regulations are Coming



On September 15, 2021, European Union (EU) Commission President Ursula von der Leyen announced the Commission's intent to ban products made with forced labor from entering the EU market. This announcement comes on the heels of guidance issued in July 2021 by the Commission and the European External Action Service on how to effectively implement supply chain due diligence.¹ Von der Leyen's statement, "[D]oing business around the world is good ... but can never be done at the expense of people's freedom and dignity," reflects a growing public sentiment that inexpensive supply chains cannot supersede human rights.² Over the past few years, numerous companies in a wide range of industries, including technology giants, global fashion brands, and consumer goods conglomerates, have faced significant backlash for failing to identify and/or address such abuses taking place within their value chains.³ These issues are also relevant to financial institutions and other members of the investment community, who should take care to ensure that the companies in which they invest are cognizant of the human rights risks associated with their value chains.

Companies are facing pressure to protect human rights in their supply chains from a range of stakeholders, including consumers,⁴ shareholders,⁵ and business partners. In addition to public pressure to address upstream and downstream human rights impacts, companies are also facing increased scrutiny from governments. As attention to human rights violations—and interest in Environmental, Social, and Governance (ESG) concerns, generally—has increased, so too has the willingness of governments to pass regulations relating to supply chain human rights due diligence. These laws generally come in two different forms: supply chain due diligence reporting requirements, which governments hope will lead to voluntary due diligence screening; and affirmative obligations on the part of companies to conduct due diligence on their supply chains.

Organizations that ignore these developments risk running afoul of both government regulators and the public at large. This can result in both regulatory sanctions and significant reputational risks. Indeed, according to a 2018 study conducted by the British Institute of International & Comparative Law and Norton Rose Fulbright, companies conducting supply chain due diligence cited legal and reputational risks and meeting investor expectations as the primary driving factors.⁶

This paper will provide an overview of the state of international, US, and European supply chain due diligence laws that companies should take into consideration to avoid the risks associated with inadequate supply chain due diligence. It will also provide guidance on measures companies can implement to comply with applicable laws, including how they can incorporate supply chain due diligence into their existing risk management frameworks.

1. European Commission, "New EU guidance helps companies to combat forced labour in supply chains," July 13, 2021, https://ec.europa.eu/commission/presscorner/detail/en/ip_21_3664.
2. Reuters.com, "EU to propose ban on products made by forced labour: von der Leyen," September 15, 2021, <https://www.reuters.com/article/eu-commission-labour-idAFS8N2O6018>.
3. Reuters.com, "Investors press companies on human rights in Xinjiang," March 30, 2021, <https://www.reuters.com/world/china/exclusive-investors-press-companies-human-rights-xinjiang-2021-03-30/>.
4. Business & Human Rights Resource Centre, "Consumers increasingly boycott products & services if they disagree with business' stance on important issues," October 3, 2018, <https://www.business-humanrights.org/en/latest-news/consumers-increasingly-boycott-products-services-if-they-disagree-with-business-stance-on-important-issues/>.
5. See Footnote 3
6. BIICL.org, "Making sense of managing human rights issues in supply chains: 2018 report and analysis," https://www.biicl.org/documents/1939_making_sense_of_managing_human_rights_issues_in_supply_chains_-_2018_report_and_analysis_-_full_text.pdf?showdocument=1.



Overview of International and Domestic Human Rights Due Diligence Laws

Regulations of human rights in supply chains are a relatively new phenomena, and there are no universal standards for conducting supply chain human rights due diligence. Over the past decade, however, the United Nations (UN) has advanced several proposals regarding business and human rights that have the potential to serve as the basis for national legislation.

UN Guiding Principles on Business and Human Rights

In 2011, the UN endorsed the Guiding Principles on Business and Human Rights to implement the United Nations "Protect, Respect and Remedy" Framework, which was developed by the Special Representative of the Secretary-General and endorsed by the Human Rights Council. The objective of the Guiding Principles is to enhance standards and practices regarding business and human rights. Additionally, it seeks to achieve tangible results for affected individuals and communities and contribute to a "socially sustainable globalization." These Guiding Principles are based on three tenets:

1. States' obligations to respect, protect, and fulfill human rights and fundamental freedoms
2. The role of business enterprises "as specialized organs of society performing specialized functions," which requires them to comply with applicable laws and respect human rights
3. The need for effective remedies for breaches of rights and obligations⁷

The Guiding Principles set forth operational recommendations for companies, including supply chain human rights due diligence. The Principles direct businesses to implement a process to identify, prevent, mitigate, and account for adverse human rights impacts, including impacts from the business' own activities, as well as those directly linked to its operations, its products, or services by its business relationships.

UN Draft Treaty on Business and Human Rights

In 2014, the UN Human Rights Council started an intergovernmental working group to develop a legally binding treaty mandating human rights due diligence. A third revised draft was published in August 2021, and the working group met in late October 2021, but it is unclear when the next draft may be issued.⁸

If passed, State Parties would agree to require businesses to conduct human rights due diligence proportionate to their size, risk of severe human rights impacts, and the nature and context of their operations.⁹ Specifically, they would be required to:

1. Identify, assess, and publish any actual or potential human rights abuses that may arise from their business activities and business relationships.
2. Take appropriate measures to prevent and mitigate identified actual or potential human rights abuses arising out of their business activities and business relationships.
3. Monitor the effectiveness of their measures to prevent human rights abuses arising out of their business activities and business relationships.
4. Report on actions taken to address human rights abuses arising out of their business activities or business relationships.

7. OHCHR.org, "Guiding Principles on Business and Human Rights," https://www.ohchr.org/documents/publications/guidingprinciplesbusinessshr_en.pdf.

8. Business & Human Rights Resource Centre, "Binding Treaty," <https://www.business-humanrights.org/en/big-issues/binding-treaty/>.

9. "State Parties" are those countries that have ratified or acceded to an international treaty.



European Regulations

The European Union (EU) also recently took steps to promote regulation of supply chain due diligence. In March 2021, the European Parliament adopted the Draft Directive on Corporate Due Diligence and Corporate Accountability. This directive would require publicly traded firms, companies of sufficient size, companies operating in certain high-risk domains, and financial services companies to take “all proportionate and commensurate measures” to prevent potential adverse impacts in three fields, including human rights, the environment, and good governance.¹⁰

While the EU does not expect member nations to implement binding laws on supply chain due diligence before 2023, several nations have already begun implementation and others already had such laws in place. The table below lays out the progress of several EU member nations and the United Kingdom (UK) in implementing laws designed to facilitate companies' taking responsibility for human rights violations occurring in their supply chains:



France

The Duty of Vigilance Act, passed in 2016, requires companies with more than 5,000 employees to implement vigilance plans to identify and prevent severe human rights violations in their business operations, including among their suppliers. The plan, and effective implementation reports, must be publicly disclosed. Companies that do not comply are liable for any harm that occurs that would have been avoided through due diligence.¹¹



Germany

The Duty of Care Act, set to go into effect in 2023, will require companies of more than 3,000 employees to implement policies to prevent human rights abuses within the company and on the part of direct suppliers. It also requires firms to implement controls to mitigate risks of human rights abuses among indirect suppliers. Companies are required to issue annual reports detailing their compliance. Firms that do not comply face large civil fines and disbarment from government contracting.¹²



Netherlands

The Child Labor Due Diligence Act, set to go into effect in 2022, will apply to all companies that sell goods or services to Dutch consumers, regardless of size or where the company is based. Companies are required to investigate whether there is reasonable suspicion that their products were made using child labor and to develop plans to prevent child labor in their supply chains. Companies are required to file declarations of compliance and face both significant fines and criminal liability for non-compliance.¹³ A broader bill that would establish a duty of care for companies registered in the Netherlands to prevent and mitigate adverse human rights along their value chain was submitted to the Dutch Parliament in March 2021.¹⁴



United Kingdom

The Modern Slavery Act of 2015 requires companies with turnover of more than £36 million to prepare an annual slavery and human trafficking statement. In the statement, the company must document the steps it has taken to ensure slavery and human trafficking are not taking place in its business or its supply chains or state that it has taken no such steps.¹⁵

10. European Parliament, "Corporate due diligence and corporate accountability," March 10, 2021, https://www.europarl.europa.eu/doceo/document/TA-9-2021-0073_EN.html.

11. Trade and Industry Code, "Article 1," <https://respect.international/wp-content/uploads/2017/10/ngo-translation-french-corporate-duty-of-vigilance-law.pdf>.

12. BMAS.de, Sorgfaltspflichtengesetz, <https://www.bmas.de/DE/Service/Gesetze-und-Gesetzesvorhaben/gesetz-unternehmerische-sorgfaltspflichten-lieferketten.html>.

13. Eerstekamer.nl, "Eerste Kamer der Staten-Generaal," February 7, 2017, <https://www.eerstekamer.nl/9370000/1/j9vkvfj6b325az/vkblq11jgyy/f=y.pdf>.

14. MVOplatform.nl, "Translation of the Bill for Responsible and Sustainable International Business Conduct," March 22, 2021, <https://www.mvoplatform.nl/en/translation-of-the-bill-for-responsible-and-sustainable-international-business-conduct/>.

15. UK Parliament, Modern Slavery Act 2015, <https://bills.parliament.uk/bills/1389>.

The United States

While the US is a global leader in sanctioning entities for human rights abuses under the Global Magnitsky Human Rights Accountability Act,¹⁶ it does not have broad laws mandating human rights due diligence. The US does, however, have laws imposing due diligence obligations on companies engaged in certain industries. For example, US Federal Acquisition Regulation (FAR) requires companies that do business with the US government to conduct anti-human trafficking due diligence and put in place a related compliance program. The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 requires companies to report on their use and sourcing of tin, tantalum, tungsten, and gold (known as conflict minerals), which finance armed conflicts and are frequently mined using forced labor.^{17,18}

The US has tried previously to implement universal supply chain due diligence standards. However, these attempts have been unsuccessful. Most recently, the Slave-Free Business Certification Act of 2020—which would require certain businesses to disclose the use of forced labor in their direct supply chain—failed to receive a vote in the 166th Congress.¹⁹ Although efforts at the federal level have not been successful, at the state level, California enacted the Transparency in Supply Chains Act of 2010, which requires any company doing business in California that has annual worldwide gross receipts of more than \$100 million to disclose what steps, if any, the firm is taking to prevent human trafficking and forced labor in their supply chains.²⁰

Preparing for Supply Chain Human Rights Due Diligence Requirements

Given the growing focus on human rights abuses in supply chains and the trend in government-issued due diligence requirements, companies should be prepared to be held accountable for violations. Most due diligence laws include penalties for companies that are not compliant. These range in scope from administrative fines to liability for human rights violations to criminal penalties. These have the potential to be significant. The EU recommends penalties “comparable in magnitude to fines currently provided for in competition law and data protection law.”²¹ Moreover, the geographic scope of the regimes varies, and several have extraterritorial effects, meaning companies that operate internationally must assess whether their operations in other countries subject them to additional due diligence obligations.

In addition to the legal risks of not complying with supply chain human rights due diligence regulations, companies face the added burden of reputational risks of non-compliance. As previously noted, global consumers are increasingly aware of human rights abuses in corporate supply chains and are willing to punish businesses for behavior that they believe is unethical. In an October 2018 survey, public relations and marketing firm FleishmanHillard found that 66% of US consumers and 80% of UK consumers say that “they have stopped using certain products or services because the company’s response to an issue does not support their personal views.”²²

While the need to incorporate supply chain due diligence into companies’ practices is growing, companies may face challenges in designing and implementing a supply chain human rights due diligence program (human rights due diligence program). Supply chains generally encompass numerous suppliers across diverse jurisdictions, and it can be difficult to engage beyond the first tier of these suppliers. Compounding this difficulty is the limited public information available regarding human rights risks in some jurisdictions.

Given these obstacles, what steps can companies take to successfully implement a human rights due diligence program? The good news is that many companies should already have infrastructure in place to support their human rights due diligence efforts.

16. Congress.gov, “Global Magnitsky Human Rights Accountability Act,” 2015-2016, <https://www.congress.gov/bill/114th-congress/senate-bill/284/text>.

17. Acquisition.gov, “Combating Trafficking in Persons,” October 2020, https://www.acquisition.gov/far/52.222-50#FAR_52_222_50.

18. SEC.gov, “Disclosing the use of conflict minerals,” <https://www.sec.gov/opa/Article/2012-2012-163htm---related-materials.html>.

19. Govtrack.us, “Slave-Free Business Certification Act of 2020,” <https://www.govtrack.us/congress/bills/116/s4241>.

20. Oag.ca.gov, “The California Transparency in Supply Chains Act: A Resource Guide,” 2015, <https://oag.ca.gov/sites/all/files/agweb/pdfs/sb657/resource-guide.pdf>.

21. See Footnote 10.

22. See Footnote 4.

8 Key Steps to Enhance Supply Chain Due Diligence Process

 <p>Perform an Assessment of Existing Resources</p>	<p>When creating a supply chain human rights due diligence program, companies do not have to do so from the ground up. It is possible to leverage existing knowledge, processes, and systems already within the firm. Many firms already have due diligence subject matter experts on hand. Leveraging existing resources will require less effort and provide for more streamlined reporting. One way to accomplish this is to assign supply chain due diligence to an already existing team, such as compliance, risk, ESG/sustainability, or procurement.</p>
 <p>Perform a Comprehensive Risk Assessment</p>	<p>A comprehensive risk assessment may need to begin with a mapping exercise to easily visualize a company's supply chain. Comprehensive risk assessments will need to be performed regularly as human rights risks evolve over time. Proper documentation of the risk assessment methodology and results, a general principle of good governance, will make updating the risk assessment easier in the future.</p>
 <p>Incorporate the Procedures into the Existing Risk Management Framework</p>	<p>By incorporating supply chain human rights due diligence procedures into an existing risk management framework, companies can leverage existing monitoring and testing procedures. Where applicable, they can develop risk prioritizations procedures for high-risk jurisdictions or activities.</p>
 <p>Assess Data and Identify Gaps</p>	<p>When creating a supply chain human rights due diligence program, it is likely that companies will have to enhance vendor due diligence questionnaires and screening procedures. If not yet in place, companies should consider implementing negative news screening and risk-based onsite visits specifically targeted at assessing compliance with human rights requirements.</p>
 <p>Review Existing Contracts</p>	<p>Companies should review all existing contracts to make sure that human rights due diligence requirements are incorporated. Contracts should also include language requiring any subcontractors to comply with said human rights due diligence requirements. While this may not always be feasible in the near term, to the extent that this process takes time, companies should engage with its counterparties to notify them of the companies' expectations and reach an understanding regarding each side's roles and responsibilities.</p>
 <p>Embed Compliance Processes into Supply Chain Management</p>	<p>Ensure that all employees are given adequate training, that suppliers provide certificates of compliance, and that whistleblowing hotlines are included in supply chain management.</p>
 <p>Stakeholder Engagement</p>	<p>Engage with stakeholders such as the employees of suppliers or communities impacted by their business operations and provide a grievance mechanism for complaints. This engagement should be strategic, tailored to the group targeted, and done in a manner that does not put the stakeholders at risk. For example, a company may work with nongovernmental organizations advocating on behalf of a particular group or trade union representatives to gain insight into the perspective of certain stakeholders or provide a way for stakeholders to report anonymously. Companies may be able to leverage their current whistleblower hotline processes.</p>
 <p>Reporting Requirements</p>	<p>As noted above, many regulations require supply chain due diligence reporting. Tailor the human rights due diligence program to the firm's business model and risk profile. It is important to ensure that any program aligns with reporting procedures.</p>

With the increased focus being placed on human rights violations in companies' supply chains, due diligence should become an important component of a company's overall risk management. While the requirements differ from one jurisdiction to another, there is a clear trend toward holding companies accountable for not only their own operations, but throughout their value chains. Firms should act to put in place human rights due diligence programs. Those companies that already have robust risk management frameworks are well-positioned to incorporate the necessary elements of a human rights due diligence program into their existing processes.



How Guidehouse Can Help

Guidehouse's team has in-depth knowledge of supply chain due diligence and investigation in the US, Europe, and globally, and understands supply chain due diligence best practices in the financial sector and beyond. Our team, composed of former compliance and risk officers, attorneys, bankers, regulators, prosecutors, law enforcement officers, and information technology professionals, brings to bear critical expertise and resources to help clients develop robust and effective compliance programs and assess their supply chain due diligence frameworks to determine whether they are operationally effective and meet regulatory expectations.

Guidehouse can review and assess your supply chain due diligence program to determine whether it is sound, to identify gaps or weaknesses, and/or to conduct training on supply chain due diligence investigations and compliance. Guidehouse is well-equipped to make an individualized assessment of your unique circumstances and offer innovative advice and solutions for responding to heightened regulatory requirements. We are also equipped to support you in a broader review of your compliance program.

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