Meeting Minutes for the APPG on Environmental, Social, and Governance

Topic: How ESG can help address modern slavery in UK supply chains and financial investments.

Date: Wednesday, 23rd February, 10.30am (Hybrid)

Chair:
Alexander Stafford MP, Chair of the APPG on ESG

Parliamentary attendees:
Gareth Davies MP, Vice-chair of the APPG on ESG

External speaker:
Dame Sara Thornton, The Independent Anti-Slavery Commissioner

Attendees:
Georgina Berriman, Policy and Communications Adviser, Corporate Justice Coalition; Maria Pia Bianchetti, Senior Specialist, Child Rights and Business, UNICEF; Alice Lucas, Policy & Advocacy Manager, The Fairtrade Foundation (attending virtually); Tom Wills, Project Manager, Corporate Accountability and Trade, Business & Human Rights Resource Centre; Madeline Young, Associate Professor & Module Leader in Economics, Anglia Ruskin University of London; Amelie de Borchgrave d'Altena, Co-Head of Corporate Intelligence, KPMG; Jade Thomas, Compliance Manager, EDF Energy.

The meeting starts at 10:30 am.
The Chairman thanked all attendees for joining the formal meeting and introduced the two speakers, Gareth Davies MP and the Independent Anti-Slavery Commissioner, Dame Sara Thornton.

Vice-chairman: Previously worked in financial services and managed ESG. The 2015 Modern Slavery Act was pioneering legislation but omitted investment portfolios. It does not account for the investment process, therefore a big gap in the regulatory agenda in relation to modern slavery. Emphasised to the group that financial services *are* making efforts to track modern slavery, but it is often not reported, simply because it is not required. Britain is the third-largest pension market in the world with £3 trillion in investable assets and the second-largest asset management industry with £9 trillion, represents tremendous power for change, If financial service companies have a stricter approach to modern slavery we can go a long way in combating this issue and the UK is in a great position to have a leadership role on this problem.

Moreover, pensions have a fiduciary responsibility to look at their investments. Since becoming an MP, has found talking with financial services that that financial institutions are mindful of modern slavery and want to tackle it. Imperative therefore that policies do not stigmatise in the market those investors that identify links to modern slavery. That kind of approach is not what this is about.

Dame Sara Thornton: I think of modern slavery in this context as the canary in the coal mine. Indeed, under the Liechtenstein initiative financial services are the lever to change global economic and financial systems. To scale up output the IASC partnered up with Themis and the TRIBE Freedom Foundation to publish in January 2021 a report on preventing modern slavery and human trafficking (an Agenda for Action across the Financial Services Sector). The IASC surveyed 51 CEOs of leading companies in the financial services sector to ask them to respond to the report. 44 organisations responded. There were examples of good practice but generally there was a lack of awareness, but acceptance has grown in the sector that it had a responsibility to investigate portfolios. The IASC offered five recommendations for financial businesses to improve their handling of modern slavery until the government legislates to extend Section 54 of the Modern Slavery Act to cover portfolios.

The first is Improving risk systems and integrating modern slavery in companies risk management to develop better risk identification, assessment and mitigation controls or to integrate modern slavery and human trafficking risk into its existing systems. The IASC also argued for more consistency in the definition and understanding of forced labour risks.

The second recommendation concerned the sharing of data: how to improve ways to share information. Typically, banks and other financial institutions cannot share information about bad actors with each other, so if someone has problems with a bank they can just go to a different bank and open an account ther and this seemed to be key.

The third recommendation concerns collective action: if we find problems we must work together to fix them. Initiatives such as CCLA's Find it Fix it Prevent are a great example of how collective action can incentivise and accelerate improvements in company disclosure and compliance to the Modern Slavery Act.

The fourth area concerns the reliance of financial services on electronic supply chains. We need to support those children in mines in West Africa mining minerals for microchips. Industry minister Lee Rowley is being cooperative on this front as part of his efforts to build resilient supply chains. The challenges of electronic supply chains stretch not only from assembly and manufacture of devices, but also of the mining of rare metals, and the manufacture of silicon.

The last point had to do with the ambiguity of the Section 54 of the Modern Slavery Act. Despite the fact that financial institutions could have a major impact against forced labour through their investment and lending portfolios, very few are disclosing this activity in modern slavery statements. Section 54 should include investment portfolios and this should be done voluntary before new legislation is introduced.

A report on modern slavery, found that only 50% of companies annual reports mentioned it. While we are doing more on risk identification and mitigation we must undertsand how are we going to mainstream modern slavery. The law is ambiguous and we we know that only 27% of asset managers do their due diligence in terms of modern slavery. In Australia the legislation is much clearer. Extending this legislation will allow financial services to do this for good.

Discussion

Chairman: On the issue of critical minerals I met with Lee Rowley recently, he said critical minerals would be part of the expression of interest. I too am concerned about stigmatisation, this needs careful consideration on the legislative side. In environmental due diligence, businesses typically only look at the beginning and do not have units looking back over the lifecycle of an investment. Is this legislative or do we need a cultural change? [To the IASC] were you surprised that some companies did not respond to you? I am interested in knowing whether companies are saying one thing and actually not doing it.

Vice-chairman: I'll take it from the financial perspective and finance firms so I will take two of those, one on the reputational piece and the bravery to come out and secondly on doing one thing and saying another. On reputational management, in my discussions with various organisations that do this full time, what they said to me was that everyone should just assume that they have exposure and go from there, rather than assuming that nobody has exposure. We should start on the assumption that particularly multinational organisations will have exposure somewhere. We also need to have a little push in legislation for the smaller firms, make it part of their risk management process, the idea behind it is that you identify before you even invest. If you are a good fund manager, you will have a very robust process for identifying material risks, the materiality of ESG risks not just to avoid reputational damage but for financial performance. Well run companies with strong governance procedures will be good investments and so as a fund manager, I would be looking for the best run companies with processes in place to ensure that they are continually monitoring their supply chains. If a company is doing that, it will be a good company to invest in. By the way, climate was not really a big deal in the city for a long time, and all of the sudden there was a big change. Part of it was French legislation under Article 174 of legislation requiring state pension funds to disclose climate exposure in their portfolios and that in turn, had a big impact in my firm because we ran a lot of money for for French state funds, we had to then look at our own portfolios and look for climate exposure and then have reports on it and I see this as very similar. If we are asking the questions to the CEOs, then they will ask their COOs what we are doing about modern slavery?

A lot of firms have told me they look at modern slavery, some have a modern slavery liason but 99% of the time that individual wasn't working in the asset management but the investment banking division, and it was in the crime and money launduring team not in the asset managent team, who were actually investing the money, so yes, applaud that they were doing something but it wasn't active, they weren't active in the division that I want them to be active in: private wealth management and asset management. Article 54 should directly address private wealth management and asset management in investment portfolios.

Dame Sara Thornton: On that last observation, I would agree with you completely, that is why when we talk about data and risk management we said it is across all business processes and if there was data around ESG, it was part of basic screening and transaction processes. NGOs and campaigners around modern slavery typically argue on the basis of salience such as human rights, that we should all be very concerned, and sometimes they have been a bit hesitant to argue that there is material risk, material to the success of a business and I have no kind of caution about arguing that is a both material and a saliance risk. Your point about that, if you haven't found it you haven't probably looked for it. I often use data from the PTI trade initiative from a few years ago. 77% of CEOs thought they did have forced labour in their supply chains. Those 77% were willing to admit that, and I think that it is there if you look for it, so a process that is about transparency and disclosure is vital. On the critical mineral strategy, I have spoken to officials about this, it is not just about electronics but solar and the green economy, because there are real real concerns that while we want to make that transition we risk bringing along a lot of exploitation, slavery and forced labour deep in the supply chains. What worried me was that the need for more solar was trumping concerns for human rights issues, I really believe we need to push. Their view was: it’s okay for the Americans to have import barriers on quite a lot of these components and solar panels but we are in a slightly different position, I think that is something that should be subjected to debate.

Chairman: A couple questions, you talked about identifiyng modern slavery, but can we talk about improving the actions against modern slavery?

Vice-chairman: One observation that I would make, and again in the conversations I have had, some companies have actually welcomed this attention because they see it as a competitive advantage that they have robust processes in place. A lot of companies now have developed their own ESG ratings and systems, this was something that I implemented at my last job. Just before I left we invested millions of pounds on the data science team to be able to quantify ESG factors which would inform our firm manager and be able to provide the data to back up decisions and analysis and I think that has come a long way but again you can only do that if you have financial resources. I do think the issue is for the smaller firms. Whenever you impose legislation and regulation on the market, inevitably the cost comes to those smaller businesses. If you are a startup or a small asset management firm it is very difficult, because there is going to be quite a lot of cost and effort to continually review processes and report on that. If you are JP Morgan or BlackRock you have an army of people, internationally. I do worry about that, so I am not giving you an answer but some firms see this as a great opportunity to be more competitive because they are able to say, when you invest with us, you are less likely to be exposed to modern slavery.

Dame Sara Thornton: In terms of finding slavery and trafficking in supply chains, I think the advice would always be, do not divest at the first sign of trouble, what you do is work with that supplier to put right what can you do to encourage human rights throughout the supply chain.

How can you encourage worker voices? How can you work with NGOs on the ground? There are a whole range of things that can be done and only as a last resort would you suggest divestment, doing so marginalises migrant exploited workers who will have no work at all and often that is even worse.

Contribution: Just to flag that the EU commission is publishing their draft law on Corporate Sustainability Due Diligence today and these laws are set to apply to UK companies in the Single Market.

In reference to the UK's supply chain reporting and 'due diligence' requirements being located in the MSA S.54 and now with different obligations, scope and enforcement across the EU the UK's approach could lead to a patchwork of rules that impose a greater compliance burden on businesses. This approach risks being less effective in terms of the underlying ESG goals than a more comprehensive and consistent approach contained within a single piece of legislation. Do you think that there is a need for a new piece of legislation that places a duty on businesses and investors to prevent not just modern slavery but all human rights abuses across their supply chains?

Contribution: UNICEF has published guidance for investors on how to integrate child rights into ESG assessments. There is also an increasing recognition of the connection between climate and human rights. Business' mitigation and adaptation efforts to climate change can also have negative impacts on child rights as recognised in the COP26 Declaration on supporting a just transition - corporate due diligence is recognised as one effective way to erradicate modern slavery and prevent child labour in supply chains. Undeniably, legislation can bring the necessary change in corporate behaviour at the scale and pace needed to eradicate modern slavery. What do the panel think of 1) going beyond climate-related disclosure to expand it to integrate modern slavery and more widely child rights abuses, especially considering the risks to children from the transition to net zero? 2) the possibility of revising the UK's approach to business and human rights by introducing a law that would oblige companies to conduct human rights and environmental due diligence, rather than just reporting, which is the approach that other countries are also taking and UK civil society and business are calling for?

Contribution: Social transformation needs to have a lot of benchmarking. Is it time for an overarching piece of business legislation that takes a holistic view of responsible business conduct by requiring companies to conduct human rights and environmental due diligence? Shouldn't we be encouraging the market to reward responsible practices – like addressing modern slavery – rather than encouraging a race to the bottom for minimum compliance?

Dame Sara Thornton: there is a great thread across those three questions which is about human rights and environmental due diligence. I don't know what the EU is going to publish because I do know there has been a big debate about who this will apply to. I am really interested in whether it will be a failure to prevent issues, a lot of people say that it needs to be akin to the Bribery Act and the failure to act. I am not absolutely persuaded that this is the right way for us yet for two reasons. If the requirement is about all environmental and all human rights issues, from a quite selfish perspective I am afraid that modern slavery will get lost, particularly when there are other things that are much easier to measure. There is some value, I think, in a modern slavery statement in the UK having to be signed off by the board. The other point is more of a principled concern, I don't quite understand how these sorts of approaches, particularly if there is a failure to prevent, sit alongside transparency, and I go back to the comments that we have all made about the approach to the Modern Slavery Act in this country has been, go look for it find it and deal with it. My worry is that if you have heavy sanctions over failure to prevent then you will just push that underground and have a very sort of cautious approach, companies' lawyers will be all over it and I just don't understand how it sits side by side with transparency, particularly if there was a failure to prevent then we would have mitigation, whether that was civil or criminal, mitigation that I think has a sheer effect on our strategy that has been about encouraging transparency.

Vice-chairman: I actually started by saying that I am not necessarily pushing for a legal change in section 54, that is one of the options. Another option might be similar to what we have done on climate change with TCF. Ultimately, for us to be able to tackle this, it needs to be a global endeavour. I would love to see Britain lead a global coalition of the biggest financial services markets on this and that we all have an agreement. My office has had a little contact with Marco Rubio's team in the US who is talking a lot about this, I know some politicians from Germany who talk about this as well, I do think there is an opportunity to coordinate the big financial services markets of the world and see if we can get a common approach that doesn't require legislation because I understand what Georgina is saying about a patchwork and that can be very costly for businesses. I would just point out that in 2015, when we did pass the Modern Slavery Act that did lead to a lot of other countries taking action. Others passed modern slavery acts, as you said France, the Netherlands and Australia but others in other countries have acted in other ways. Australia went further than we did and has implemented section 54 for investment portfolios so that is also a benchmark. I think Britain is leading on this and has a leadership role to play more so than the EU in my view just because of the size and sophistication of our market compared to any other country in the EU financial services sector.

I dont think that anyone in the investment community wants to be supporting in any way child labour or modern slavery as I said, the issue with ESG has been, historically a lack of ability to quantify these issues but also to identify. Climate is a lot easier, you can measure it. That is problematic for two things. One - identifying - but two - overseeing and adjudicating on performance of their action on this. One thing that drives me bonkers in certain parts of this market with charities and NGOs and people who haven't actually come from finance is that they start from the presumption that everyone in finance is big and bad and just trying to screw over the world and the planet to make a buck. It could not be further from the truth. We should start from the presumption that good investments come from investing in good companies, and it is not always the case that it is easy to identify issues, it is because of that and not because there is some big fat cat in the City of London or in New York trying to screw over the planet. Any legislation to oppose this more broadly, is not in line with free market principles which we are all trying to adhere to in advanced democracies and is not required because good businesses will act.

Contribution: Your point about quantifying social impact. They are not quantitative, they are qualitative, and that requires a huge amount of leg work and requires discussion because we are human right? And I think that is where we are having a lot of difficulty. How do you have that qualitative data and the diversity of types of dialogue that we need to have with people? For those of us on this call and in this group who have done community surveys of people who are impacted by business activities, civil societies, verbal, vocal, global, they are supported by all the international NGOs who connect with all the most competent people in every single small country of the world. They are there and they want to talk to us, they are on Facebook, on Twitter but those conversations are really uncomfortable and they have a lot of demands. Some of those are linked to business activities and some of them are linked to their governments not providing public services. Making that distinction, that is a discussion that we do not want to get into often because it is contentious. How do we address that lack of dialogue? It's an uncomfortable, gritty, human discussion. You need linguistic capacities, you need decentralised people in those countries with those languages. That is a lot of what is missing, we don't know the human impacts because we do not have that data. The second one is the inherent risk of rising financial inequality. We have rising inequality, including in the most wealthy countries and middle income countries, that comes from the UN world social report of 2020. We have a desire to drive down production costs, we have increasing wealth, we also have consumers wanting lower costs, that is an inherent risk for modern slavery. Our low wage workers are the lowest and then below that are unpaid people. So that increasing global inequality is a holistic global issue particularly for the wealthiest countries to address. So how do we get the government's macroeconomic policy to address rising inequality which is what pushes modern slavery and lower wage work which is what ESG is trying to address. Climate change, wealthier people have a higher carbon footprint. How do we do that holistically?

Contribution: We spent five years tracking modern slavery statements put out by companies. The Modern Slavery Act, in terms of driving disclosure was failing against its own stated objectives. We also recently published an analysis of the Australian model of the Slavery Act, finding that although it does go further, as you said, it has also not succeded in driving transparency to anything like the scales stated. As you said, most of the companies, in their own right, are already reporting but unfortunately, in the UK 40% consistently fail to follow the law and I'd be interested to hear your thoughts. Our thoughts, for what it is worth, is that the Modern Slavery Act in itself is not a suitable vehicle and we point to what was already said about the human rights due dilligence efforts made in the EU.

Dame Sara Thornton: On your point about quant/qual, yes it is very difficult but it has to be done, and my view is that a lot of campaigners and NGOs have wanted to stay in this salience area, but we need to be able to count it materiality, we need to have a framework, we need to be able to benchmark. It has taken twenty years to get anywhere near that on carbon, it takes a long time but we need to do it. So absolutely with you but I completely agree that it takes difficult conversations. On your point about global inequality, I think that is why it is very important that in 2015, the UN sustainable development goals included a commitment to the eradication of modern slavery because that moved modern slavery into a development issue and there was a really good piece of work published by the UN last year which linked investment in modern slavery initiatives to development goals and addresed why the two are very important so I completly agree with that. About Australia, the Australian legislation is probably 85% - 95% the same as ours, they just did it two or three years later and it is better because they learnt from us, in the area of investments, it absolutely is covered, it is explicit. We have gone through the Modern Slavery Act, we've taken the approach of transparecy, it is five or six years old. I am concerned about moving to the latest kind of sweet shop which is human rights due diligence without any sense of how it would work, how it would apply because it just seems to be that it is the latest idea, and I have reservations about how it fits with transparency and how it fits with modern slavery. I am not quite there but I am very aware that there are campaigns to say that it is the answer. If I wanted to be sceptical, of course campaigners have to sell a simple answer, I just think it is a lot more nuanced and complex than that.

Vice-chairman: So on the qualitative aspect, you are totally right. What it comes down to is engagement, what I am interested in is asset management. As I have said, I think it would be most useful to target the largest asset managers but you can only go so far. A large asset manager is not going to invest in certain countries, certain markets and certain companies, mostly publicly listed companies in very developed or developing, emerging markets. So there is only so far you can go with this but engagement is the key for this. On inequality, it is about globalisation and cheap labour and I think that is a whole other discussion about what we can do to reduce inequalities, and this is not the place to do that but that does not mean that it is not important. Correct on enforcement, this one of the biggest issues with modern slavery and I know that is what the Home Office is focused on in terms of new legislation and improving the Act. I want us to give it a chance actually on this Act, I think that is the plan. We already have legislation on this, let's make it better rather than scrapping it and trying something new. The Modern Slavery Act of 2015 was always a starting point, not an end point and I think it would be really good if we could all work together to make this legislation that we already have more impactful and better than it is today and I think that is where the government is as well.

Chairman: Thank you both for joining, great conversation, thank you everyone for joining, the secretariat will email you about various stuff that is happening. Our next meeting is on Wednesday, 16 March at 10.30am. It is a discussion about the landscape of green finance regulation.