



MAY 21

**RESPONSIBLE BUSINESS**

# Legal due diligence and human rights

## The role of companies and M&A lawyers

Legal due diligence processes are widely known in the context of mergers and acquisitions (M&A) and corporate reorganisation projects. Their aim is to analyse the operations and organisation of companies to identify their degree of compliance with applicable legal and contractual regulations, the level of risk of non-compliance, and the potential sources of legal and contractual liability.

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But, these days, is it still enough to adopt a purely legal and financial approach in M&A due diligence processes?

Everything leads us to conclude that no, it is no longer enough.

We live in a world where corporate social responsibility and the economic, social and environmental sustainability of businesses take centre stage, and one of the pillars of this new paradigm is respect for and protection of human rights.

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All companies, regardless of the sector in which they operate, their size or geographic location, are increasingly required to do business in a way that respects human rights. They are also required to be proactive in promoting environmental and social causes. In this context, there is an enormous pressure, perhaps even a demand, for companies to act in compliance with the main internationally recognised soft law instruments. These include the Universal Declaration of Human Rights, the International Covenant on Civil and Political Rights, the International Covenant on Economic, Social and Cultural Rights and the International Labour Organisation Declaration on Fundamental Principles and Rights at Work. They also include other instruments whose relevance may be greater or lesser depending on the area in which the company operates. We would also highlight the United Nations Convention on the Rights of the Child and the United Nations Convention on the Rights of Women.

These instruments were joined in 2011 by the United Nations Guiding Principles on Business and Human Rights, which expressly and clearly established obligations for companies in terms of human rights. Among the measures that companies should adopt, Guiding Principle 17 sets out the duty to carry out human rights due diligence processes.

In this movement, some countries have gone further and created pieces of legislation that impose obligation on businesses to monitor and implement human rights due diligence programmes. Examples include the French Corporate Duty of Vigilance Law, the Transparency in Supply Chains Act applicable in California since 2010, the Australian Modern Slavery Act 2018, and the UK Modern Slavery Act 2015.

The issue of human rights has thus appeared on the radar of companies, both in the context of their business activities and in the commercial relationships they establish, where there is also a more general duty of due diligence, and in the M&A deals they consider.

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It has become inevitable and necessary for due diligence processes in M&A projects to take into consideration this new corporate duty. As a result, there is a new lens to assess companies and their impact on society has emerged, the lens of human rights.

At this point, the following questions arise: How should we structure and organise human rights due diligence processes in an M&A transaction? How can an M&A lawyer contribute to this cause? How can we guide clients on this issue?

**How should we structure and organise human rights due diligence processes in an M&A transaction?**

The way forward is to include the identification of sources of risk and potential violations in matters of human rights in M&A due diligence processes. These processes should also identify (preventive and/or corrective) solutions for the situations identified. Therefore, information should be requested and companies should be prepared to provide full disclosure on these matters. This includes information on how they operate, deal with their employees, impact the community around them, contribute to a more sustainable world, and guarantee that their commercial partners, clients and suppliers adopt and respect identical principles.

The analysis of these matters in a due diligence process should take into consideration not only the company's own activity and projects, but also those of its subsidiaries, which may be located in countries with less demanding practices regarding these issues. It should also consider the third parties the company interacts with, such as suppliers, members of the production and distribution chain, and customers, etc.

**How can an M&A lawyer contribute to the management of the risks involved?**

Not all M&A lawyers are expected to become human rights specialists. However, in the context of due diligence and risk assessment when buying or selling companies and assets, these matters have a critical relevance today that is not expected to diminish.

Possible human rights violations are contingencies to be considered in the sale or purchase of companies and assets. In fact, this area will be no different from other areas of legal or financial risk typically dealt with in these processes. Integrating this topic in the context of an M&A process is the way forward and the train is already leaving the station.

From a more practical point of view and based on the experience we have accumulated, M&A teams should consider the following concerns in this area:

ACQUISITION OPERATIONS:	DIVESTMENT OPERATIONS:
Are there any serious human rights violations that the seller has caused or contributed to in the past that should be addressed in the transaction? If so, we recommend, for example, that (i) sellers remedy the situation before the transaction closes; (ii) the transaction be aborted or the price affected; (iii) buyers take corrective action after the closing.	Are there any serious violations that were caused by or contributed to by the divested company that should be corrected before the divestment, or whose regularisation should be agreed upon as a responsibility of the buyer to be implemented after the closing of the transaction?
Are there any serious human rights violations (e.g., the purchase of raw materials from suppliers using child labour, disrespect of gender equality, wage differences due to discriminatory practices, negative social impact on local communities, reprehensible environmental practices, etc.) that should be raised during the negotiations? And are there any practices that should be reported to external entities?	Can sellers influence the buyers' policies and plans for the divested business in order to maintain good practice in human rights protection for the future?



Thinking about this issue makes us believe that, as M&A lawyers, we can play an important role in obtaining information, and in researching and questioning company practices. By doing this, we can contribute to companies being responsible in terms of human rights and to permanently monitoring their compliance levels.

### How can we provide guidance to clients on this issue?

Introducing this new dimension into M&A due diligence processes is a challenge, but the advantages for our clients are undeniable. Here, we take a look at some of them:

- **Corporate Responsibility** – allows companies in general and even those of a smaller size or located in less active geographical areas, to be aware of this issue for the benefit of the communities in which they operate.
- **Adoption of best practices** – companies will be asked to organise and provide information on these issues, in transparent way. This will lead to companies feeling obliged to think about this concept, discuss their past practices and (re)define future practices, in a timely and balanced manner.

- **Reputational impact** – makes it possible to strengthen trust with customers, investors, stakeholders, and business partners, as well as governments, the community, consumers and the media. This will translate into an economic and competitive advantage.
- **Preventive / corrective reaction** – makes it possible to identify possible violations and, immediately, to adopt preventive and corrective actions for the situations identified. This strengthens business value.

This is an important challenge for our clients, but also for us. Based on our experience, together we can create a more responsible business fabric that benefits our local communities and, hopefully, contributes to a better world. ■