Responsible Business Conduct and Sustainable Finance in the Philippines

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This resource document sets out how a Responsible business conduct lens in the context of ongoing sustainable finance considerations in the Philippines could be a practical way to engage the private sector in broader government policy objectives. It provides an overview of conceptual links between sustainable finance, corporate governance and RBC, as well as recommendations on how to support RBC and sustainable finance in the Philippines.

Responsible Business Conduct

Responsible business conduct (RBC) centers around an expectation that all businesses – regardless of their legal status, size, ownership structure or sector – avoid and address negative consequences of their operations, while contributing to sustainable development where they operate. This means integrating and considering environmental and social issues within core business activities, including throughout the supply chain and business relationships. A key element of RBC is risk-based due diligence – a process through which businesses identify, prevent and mitigate their actual and potential negative impacts and account for how those impacts are addressed. Many businesses also find that responsible business is good business, beyond ensuring respect for human rights and compliance with relevant laws and regulations. Understanding, addressing, and avoiding risks material to business operations in a more comprehensive way – that is, beyond financial risks – can often lead to a competitive advantage.

RBC expectations are now prevalent throughout global value chains and public expectations on RBC and are also rising. OECD instruments on RBC are being embedded into policy and legislation[1] and trade schemes are increasingly integrating social, labor, and environmental provisions.[2] Key export markets are integrating RBC standards on supply chain due diligence in mandatory and voluntary regulations, and groups of investors are monitoring RBC due diligence implementation across companies in their portfolios and calling for RBC due diligence amongst corporates.[3]

RBC is also fundamental to building resilient, inclusive and sustainable economic growth. The COVID-19 crisis has exposed significant vulnerabilities in company operations and in global value chains, including disaster preparedness and supply chain continuity and resilience. Rebuilding trust in national and regional markets in response to the Covid-19 pandemic requires strategies to build more resilient and inclusive value chains – strategies that ensure the security of supply in essential goods, and the

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[1] OECD, Policy trends in environmental due diligence, 2021. Examples include EU Proposal for a Directive on corporate sustainability due diligence, France Corporate Duty of Vigilance Law, US Dodd-Frank Act, German Supply Chain Due Diligence Act, EU Directive on Non-Financial Reporting, Australia Modern Slavery Act.

[2] See for instance the European Commission legislative proposal for a new EU GSP trade programme (for 2024-2034), which incorporates a number of changes relating to the scheme's social, labour, environmental and climate provisions, and the trade and sustainable development (TSD) chapters in EU free trade agreements

[3] In this respect, over 100 institutional investors representing over 5 trillion USD AUM have called for a mandatory due diligence law. Additionally under the EU Sustainable Finance Disclosure Regulation asset managers will have to report on their due diligence policies as well as exposure to principle adverse impacts at a portfolio level.

strengthening of business capacity to better anticipate and manage shocks whilst protecting workers and the environment.

Box 1. OECD Instruments on Responsible Business Conduct

The OECD Guidelines on MNEs is an international soft law instrument that provides non-binding principles and standards for responsible business conduct, backed by 50 governments representing 61% of global trade and 80% of international investments. They enshrine recommendations from governments to business on how companies should be contributing positively to sustainable development, while also addressing their adverse impacts on people and the planet. This includes recommendations for responsible business behavior across all areas of business impact, including but not limited to the environment, industrial relations, consumer interests, disclosure and science and technology.

Specifically, the Guidelines set out the expectation that business conduct comprehensive supply chain due diligence to identify and address adverse social and environmental impacts. The OECD Due Diligence Guidance for Responsible Business Conduct provides practical support to enterprises on the implementation of the OECD Guidelines by providing plain-language explanations of its due diligence recommendations and associated provisions. The OECD has also developed due diligence guidance for specific sectors including for the financial sector. This Guidance can be useful for business and financial institutions in improving risk and reputation management; obtaining the social license to operate; protecting brand capital; promoting market access, as well as operational efficiency and productivity gains.

Sustainable Finance, Corporate Governance and RBC

Sustainable finance refers to the process of incorporating environmental, social and governance (ESG) considerations into investment decisions. Different forms of sustainable finance are increasing rapidly due to increasing demand on institutional and retail investors to better reflect sustainability issues in their investment choices. The volume of "responsible" or "sustainable" financial products and strategies has grown significantly in the past 10 years, with forms of ESG investing on track to exceed a combined $50 trillion by 2025 (Bloomberg, 2021).[4] The collective assets under management represented by UNPRI signatories alone stands at US$103.4 trillion (2020) across 3038 signatories.[5]

ESG investment approaches reflect investor efforts to make better use of non-financial information to guide asset allocation decisions to improve long-term value, while also better aligning portfolios with sustainability and climate-related objectives. In particular, growth in ESG investing is being driven by demand from investors and civil society to better understand how ESG risks and impacts are being managed by businesses. This trend also reflects policy signals from governments that the financial sector should be a driving force in achieving global sustainability agendas.[6]

Making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development is one of the central objectives of the Paris Agreement.[7] Shifting social expectations and adapted policy goals has led to increasing action by governments and business to align

[4] ESG Assets Rising to $50 Trillion. Bloomberg, 2021. https://www.bloomberg.com/company/press/esg-assets-rising-to-50-trillion-will-reshape-140-5-trillion-of-global-aum-by-2025-finds-bloomberg-intelligence/

[5] UNPRI, Enhance our global footprint, https://www.unpri.org/annual-report-2020/how-we-work/building-our-effectiveness/enhance-our-global-footprint

[6] OECD (2020), "Promoting responsible lending in the banking sector: The next frontier for sustainable finance", in OECD Business and Finance Outlook 2020: Sustainable and Resilient Finance, OECD Publishing, Paris, https://doi.org/10.1787/d5c54bd6-en.

[7] Paris Agreement, Article 2, Paragraph c. 2015 https://unfccc.int/process-and-meetings/the-paris-agreement/the-paris-agreement

investment decisions with the goals of the Paris Agreement in particular,[8] for example, at both domestic and regional levels through the International Platform on Sustainable Finance,[9] and the Network of Central Banks for Greening the Financial System.[10]

Sustainable finance, as a practice and policy concept, is on the rise globally. In the Asia-Pacific region, sustainable finance markets are maintaining rapid growth with significant focus on the need for a sustainable economic recovery from COVID-19. In ASEAN, financial institutions and investors issued a record high number of green, social and sustainability bonds and loans in 2020 – reaching USD 29 billion (a 5.2% growth compare to 2019).[13]

Box 2. Understanding the ESG landscape

"Environmental, social, and governance" (ESG) criteria is the term normally used by financial institutions to describe the set of criteria they use when assessing the sustainability performance of a company. While no formal, widespread definition exists for "ESG" and there is diversity with respect to how these concepts are applied by financial institutions and intermediaries, they often pertain primarily to environmental and social risks, which also pose financial risks.[11]

Financial institutions have also been applying responsible business conduct (RBC) standards by carrying out risk-based due diligence, a process through which investors are be able to avoid negative impacts of their investments on society and the environment. They are also be able to avoid financial and reputational risks, respond to the expectations of their clients and beneficiaries and contribute to global goals on climate and sustainable development.[12]

The scope of RBC and ESG criteria are highly related. Both relate to understanding and quantifying the impacts of business activities on environmental and social issues. However, RBC is specific to the standards and recommendations set out in the MNE Guidelines and pertains primarily to impacts to the environment and society, independent of financial materiality. Investors should seek to understand the content of Guidelines and assess the differences to ensure they understand the overlaps and differences.

Asia-Pacific financial markets also witnessed the diversification of sustainable finance instruments and products ranging from green, social, sustainability or transition bonds. This has also been coupled with a diversification of actors and issuers, such as Development Financial Institutions (DFIs), government pension funds, municipalities and central banks.[14] Asian stock markets are increasingly integrated,[15] and a growing share of public equity investments are being made across borders. Companies are also taking advantage of foreign equity markets to raise capital. At the end of 2018, there were 510 Asian

[8] Achieving the goals of the Paris Agreement requires ambitious action by the private sector to reduce greenhouse gas (GHG) emissions, strengthen the climate resilience of companies to adapt, and ensuring finance flows are consistent with a pathway towards low greenhouse gas emissions and climate-resilient development; The Paris Agreement; http://unfccc.int/paris_agreement/items/9485.php

[9] Objective is to scale up the mobilisation of private capital towards environmentally sustainable investments; European Commission; https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/international-platform-sustainable-finance_en

[10] Network for Greening the Financial System, https://www.banque-france.fr/en/financial-stability/international-role/network-greening-financial-system

[11] OECD (2020), OECD Business and Finance Outlook 2020: Sustainable and Resilient Finance, OECD Publishing, Paris

[12] OECD (2017), Responsible business conduct for institutional investors: Key considerations for due diligence under the OECD Guidelines for Multinational Enterprises

[13] Climate Bonds Initiative: ASEAN Sustainable Finance State of the Market 2020.

[14] ASEAN Sustainable Finance State of the Market 2020 Climate Bonds Initiative

[15] OECD (2019), Equity Market Review of Asia 2019, OECD Capital Market Series, Paris, http://www.oecd.org/daf/ca/oecd-equity-market-review-asia.htm

companies listed on a market other than the domicile of the company without having a domestic listing.[16]

The relationship between corporate governance, responsible business conduct and the environment is receiving particular attention from policy makers. Sustainable finance can support good corporate governance practices including the management of ESG risks, and harnessing the contributions of different stakeholders, be it shareholders, employees, creditors, customers, suppliers, or adjacent communities, to support the long-term success of the corporation.[17]

New initiatives on sustainable corporate governance are broadly aimed at promoting corporate governance models which move away from short-termism, shareholder primacy, and understandings of corporate purpose and fiduciary duties which focus narrowly on profit maximization. Instead, they seek to promote models which take into account broader stakeholder (including environmental and societal) interests, integration of social and environmental objectives in addition to profit considerations into business models and strategy. The introduction of penalties for non-compliance with new national regulations is also shifting legal responsibility not only for management but also for board oversight.

Philippines landscape

The Philippines has a long history of promoting corporate social responsibility and has made significant recent strides in further developing its sustainable finance and corporate governance frameworks. The Philippines is taking an active role in promoting sustainable finance through its Sustainable Finance Roadmap (2021) for instance, developed with the Philippines Inter-Agency Technical Working Group for Sustainable Finance (ITSF).[18] The Roadmap details high-level actions for a whole-of government approach to promoting sustainable finance. Objectives include the development of public policy to provide strategic direction and incentives to accelerate sustainable finance, and investment to support a transition to a sustainable economy.

In 2020, the Central Bank of the Philippines (Bangko Sentral ng Pilipinas or 'BSP') approved a Sustainable Finance Framework (BSP Circular No. 1085), which sets out that all banks in the Philippines are expected to integrate sustainability principles covering environmental and social risks in their corporate governance and risk management frameworks, as well as their strategic objectives and operations.[19] The Philippines' Securities and Exchange Commission (SEC) Memorandum Circular No.4, 2019 further requires publicly-listed companies to report on sustainability-related issues,[20] and promotes reporting in line with leading disclosure frameworks such as the Global Reporting Initiative's and the Task Force on Climate-related Financial Disclosure. Under the Code of Corporate Governance for Publicly-Listed Companies, corporate boards are responsible for establishing a clear disclosure policy for non-financial information, with an emphasis on the management of economic, environmental, social and governance issues underpinning sustainability.[21]

Government-owned and controlled corporations are required to be socially responsible and to act as

[16] OECD Equity Market Review ASIA 2019 https://www.oecd.org/corporate/ca/OECD-Equity-Market-Review-Asia-2019.pdf
[17] OECD Business and Finance Outlook 2021, https://www.oecd.org/daf/oecd-business-and-finance-outlook-26172577.htm
[18] Philippine Sustainable Finance Roadmap. 2021 https://www.dof.gov.ph/wp-content/uploads/2021/10/ALCEP-Roadmap.pdf
[19] BSP Circular No. 1085. Banko Sentral ng Pilipinas. 2020. See: https://www.bsp.gov.ph/Regulations/Issuances/2020/c1085.pdf
[20] Memorandum Circular No.4, Series of 2019 on the Sustainability Reporting Guidelines for Publicly-Listed Companies. Available here : https://www.sec.gov.ph/mc-2019/mc-no-04-s-2019-sustainability-reporting-guidelines-for-publicly-listed-companies/
[21] Code of Corporate Governance for Publicly-Listed Companies, 2016, https://www.sec.gov.ph/wp-content/uploads/2019/11/2016_memo_circular_no.19.pdf

good corporate citizens under the Code of Corporate Governance for Government-Owned or Controlled Corporations.[22] In response to the COVID-19 crisis, the Government also created a new Governance Commission to serve as an oversight body for government-owned or controlled corporations and to support greater alignment with national development policies and programs. [23]

Philippines has also supported regionalizing these efforts. The critical role of sustainable finance has also been recognised by the ASEAN Finance Ministers and Central Bank Governors.[24] The BSP, in partnership with other ASEAN central banks and monetary authorities, issued a series of recommendations on the Roles of ASEAN Central Banks in Managing Climate and Environment-related Risks in 2020, which recommended embedding environmental, social and governance standards into central bank operations and strategies. [25] ASEAN finance bodies are introducing a common language across ASEAN for financing sustainable economic activities known as the ASEAN Taxonomy[26] to help guide investments towards activities that can promote the transition of the real economy onto a more sustainable footing.[27] These trends echo developments observed elsewhere. The EU for instance recently introduced a taxonomy to reflect commonly agreed principles and metrics for assessing whether economic activities can be considered environmentally sustainable for investment purpose, and Japan's revised Corporate Governance Code includes new benchmarks on sustainability.

Whilst progress in developing public policy has advanced in certain areas, businesses in the Philippines are having to address a range of new economic, social and environmental risks and challenges resulting from COVID-19 and the climate crisis. As the situation evolves, new risks will inevitably emerge or become more salient, and companies, their shareholders and society at large, all have an interest in their proper identification, management and disclosure. Whilst certain investors have taken actions to integrate climate change and sustainability concerns into investment decisions and portfolio allocations, greater clarity is still needed on how to manage sustainability risks is needed for ESG practices to support market efficiency and integrity.

Considerations and resources

Over the past five years, the OECD has worked to translate how different RBC standards and principles apply to different sectors,[28] including in the financial sector – leading to the publication of RBC guidance addressed to financial sector practitioners. The *Responsible Business Conduct for Institutional Investors* (2017) and *Due Diligence for RBC in General Corporate Lending and Securities Underwriting* (2019) provide clear and practical guidance on how to create governance systems that identify, respond to, track and publicly report on environmental and social risks and impacts associated with business activities and relationships (or investee companies and clients across portfolios and strategies).

OECD standards on RBC provide an authoritative framework on how ESG issues should be defined across markets. "RBC" and "ESG" criteria both relate to environmental, social and governance considerations, which are at the core of sustainable finance. These recommendations are not limited to "impact" investment strategies or financial products with sustainability objectives, but set out

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[22] GCG Memorandum Circular No. 2012-07, Code of Corporate Governance for GOCCs. See: https://gcg.gov.ph/files/EfLOGYvaCTAqoJZDqTZG.pdf
[23] https://gcg.gov.ph/files/pKzvXoLqG7l4tpt5DuBR.pdf
[24] See for instance the ASEAN Finance Ministers' and Central Bank Governors' Meeting (AFMGM) in 2019. https://asean.org/wp-content/uploads/Joint_Statement_of_the_7th_AFMGM.pdf
[25] Report on The Roles of ASEAN Central Banks in Managing Climate and Environment-related Risks. 2020. https://www.bsp.gov.ph/Media_And_Research/Media%20Releases/2020_12/news-12052020b1.pdf
[26] ASEAN Taxonomy for Sustainable Finance – Version 1. https://asean.org/asean-sectoral-bodies-release-asean-taxonomy-for-sustainable-finance-version-1/
[27] The ASEAN Taxonomy for Sustainable Finance, 2021: https://asean.org/wp-content/uploads/2021/11/ASEAN-Taxonomy.pdf
[28] The OECD MNE Guidelines and the OECD Due Diligence Guidance for RBC.

expectations that are applicable across mainstream investment and lending activities. These standards were developed in close consultation with a multi-stakeholder advisory group of over 50 organisations, including leading global banks and expert stakeholders, and endorsed by the 50 governments that adhere to the OECD MNE Guidelines. In parallel and in recent years there has been a rise of submissions involving the financial sector to OECD National Contact Points (NCPs), the grievance mechanism attached to the OECD Guidelines for Multinational Enterprises.[29]

G20 Finance Ministers and Central Bank Governors also approved a Sustainable Finance Roadmap in 2021[30] which includes targets greater consistency, comparability and interoperability of ESG metrics, and alignment of metrics and ratings against OECD RBC standards to improve assessment and management of climate and sustainability risks and to promote a common understanding of how to address sustainability risks and opportunities across markets.

Integrating RBC standards into public policy frameworks can support coherent, consistent, robust approaches across national and international markets on how corporates address environmental and social risks and conduct sustainability reporting, which can otherwise be challenging for companies that deal with different legal and regulatory sustainability frameworks across multiple markets.

For example, the Government can promote a green recovery from Covid-19 by investing in green and resilient infrastructure and energy, which may reduce future liabilities caused by natural disasters and climate change. Investments in clean energy and connectivity infrastructure can have positive impacts on climate as well as a multiplier impact on economic growth. However, a net positive development benefit of infrastructure investment is not automatic; infrastructure projects are complex, with long supply chains and multiple stakeholders, vulnerable to corruption and other social and environmental risks.

Clean energy can deliver significant benefits, including short-run positive economic multipliers if the development of energy infrastructure is delivered in line with RBC standards. Green investments should result in good jobs and reduce negative environmental and health impacts, as well as reduce future environmental clean-up and climate change mitigation costs.[31] Meaningfully integrating environmental and social issues across all steps of the infrastructure project life-cycle, thus, becomes as much of an economic incentive as a broad sustainability goal for both governments and businesses involved in the financing and delivery of infrastructure.[32]

Financial institutions including development finance institutions (DFIs), can play a key role in contributing to social, environmental and development objectives through enabling provision of financing towards key services, infrastructures and technology. By promoting RBC amongst their clients and undertaking due diligence processes, financial institutions can avoid financing projects or assets that may be associated with harm to workers, communities or the environment, and engage and take action to help mitigate and reduce harmful environmental impacts to support the transition to a low carbon economy in line with the 2021 Philippine Sustainable Finance Roadmap.[33]

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[29] National Contact Points (NCPs) are set up by governments that have adhered to the OECD Guidelines for Multinational Enterprises (the Guidelines). NCPs have two main objectives: to promote the Guidelines and handle enquiries, which means that NCPs: 1) organise and participate in events related to RBC to raise awareness of the Guidelines and respond to questions about the Guidelines; and 2) provide a grievance mechanism to resolve cases (known as "specific instances") relating to non-observance of the recommendations of the Guidelines. To date over 500 specific instances have been filed with NCPs.

[30] G20 Finance Ministers and Central Bank Governors Sustainable Finance Roadmap, Oct 2021, https://g20sfwg.org/wp-content/uploads/2021/10/G20-Sustainable-Finance-Roadmap.pdf

[31] Philippines Economic Update December 2020: Building a Resilient Recovery. World Bank. 2020. https://openknowledge.worldbank.org/bitstream/handle/10986/34899/Philippines-Economic-Update-Building-a-Resilient-Recovery.pdf

[32] Responsible Business Conduct and Development Finance. Global Forum Session. 2018

[33] The Philippine Sustainable Finance Roadmap, 2021: https://www.dof.gov.ph/wp-content/uploads/2021/10/ALCEP-Roadmap.pdf

The OECD is actively engaged in ensuring quality infrastructure investments are aligned with international standards including the OECD Guidelines for Multinational Enterprises, the G20/OECD Principles of Corporate Governance and the Equator Principles, through the Cebu Action Plan[34] and the Blue Dot Network[35] for instance. Alignment here is particularly important as ESG factors become increasingly financially material and grow in importance to investors and businesses. The OECD is also supporting the SEC, the BSP, the Department of Energy and other key partners and market multipliers in the Philippines through the [OECD Clean Energy Finance and Investment Mobilisation (CEFIM) programme] for instance, through which it is helping to mobilise finance and investment for clean energy infrastructure and the delivery of development targets and sustainable finance goals. [36]

Going forward, to support the financial sector, the Government could consider strengthening expectations on ESG risk management and due diligence in lending transactions in line with international RBC standards. It could further promote sustainability reporting requirements that include the disclosure of sustainability risks, RBC due diligence strategies and targets, as well as performance against those targets, streamlined across banks, corporates and investors. Metrics and methodologies in line with international RBC standards will facilitate consistent, reliable measurement and management of ESG risks and help direct project-finance and investment to fund sustainable economic activity.

The Covid-19 pandemic has brought increased attention to the importance of identifying systemic risks and unexpected shocks in the Philippines, and led to raised awareness of the importance of resilient supply chains, business models and systems. A corporate sector that is willing and able to identify and mitigate different types of risk is at the very heart of a dynamic and resilient economy.

The heightened materiality of RBC-related risks such as climate change requires them to be fully integrated and internalized into the core strategy, operations and governance of financial institutions and corporations, and the Government can utilise international RBC standards to direct investment and business models towards sustainable projects and activities.

The role of government agencies such as the SEC on issues around risk management, corporate governance and sustainability disclosure is critical to the development of business capacity to build resilience supply chains. Continued promotion of RBC in policy and governance frameworks will support companies and communities in dealing with existing and future crises, and help deliver a more sustainable, open and inclusive economy.

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[34] https://www.apec.org/meeting-papers/sectoral-ministerial-meetings/finance/2015_finance/annexa

[35] At the request of the OECD Member States of the United States, Australia and Japan, the OECD's Trust in Business Initiative coordinates technical support on the Blue Dot Network.

[36] The CEFIM Programme is focusing on strengthening domestic conditions to attract finance and investment to support i) renewable sources of energy and ii) improved energy efficiency in buildings. CEFIM aims to help Central and Southeast Asian countries better reconcile their infrastructure investment decisions with long-term commitments such as the Paris Agreement and SDGs.

Resources

- (*forthcoming*) OECD Draft Recommendation on the Role of Government in Promoting Responsible Business Conduct
- (*forthcoming*) OECD Guidance on RBC and key considerations for carrying out due diligence for project and asset finance transactions
- OECD (2019), Due Diligence for Responsible Corporate Lending and Securities Underwriting: Key considerations for banks implementing the OECD Guidelines for Multinational Enterprises http://mneguidelines.oecd.org/due-diligence-for-responsible-corporate-lending-and-securities-underwriting.pdf
- OECD (2018), National Action Plans to Enable RBC Policy Coherence. https://mneguidelines.oecd.org/global-forum/2018-GFRBC-Session-Note-The-Role-of-NAPs-Policy-Coherence.pdf
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- OECD (2011), OECD Guidelines for Multinational Enterprises. Available in multiple languages at https://mneguidelines.oecd.org/mneguidelines/

Promoting responsible supply chains in Asia

This workshop was held under the Responsible Supply Chains in Asia (RCSA) programme[37]*which is implemented together with Organisation for Economic Co-operation and Development (OECD) and the International Labour Organisation (ILO) and funded by European Union. The RSCA programme aims to promote respect for human rights, including labour rights, and responsible business standards in global supply chains.*

This programme is carried out in partnership with Japan (an OECD member) and five partner economies, namely the Philippines, China, Thailand, Viet Nam, and Myanmar.

[37] http://mneguidelines.oecd.org/globalpartnerships/responsible-supply-chains-asia