

# Precept 12. Role of International Companies

## *Technical Guide*

***All extraction companies should follow best practice in contracting, operations and payments.***

### **1. Introduction: Objectives and Guiding Principles**

Companies can adopt policies that protect their commercial interest while also contributing to the positive development impact of extraction for resource-rich countries. International conventions and norms raise strong expectations of corporate behavior that go beyond legal minimalism, just as the responsibilities of companies go beyond the boundary fence; best practice should include respect for the human rights of all affected by their operations. Meeting these expectations is an important part of Corporate Social Responsibility; retaining the social license to operate helps to secure a return on investment.

Terms that become widely seen as unfair or illegitimate can lead to costly interruptions of production or even expropriation. Extractive companies may have much more information, greater leverage and more negotiating resources than the government that controls the resource. Under these circumstances, the quest for a competitive edge can tilt into outright exploitation. Such an outcome can be counterproductive over the life of an individual project and costly for the reputation of the company when seeking to pursue future operations.

The framework presented by John Ruggie, the UN Secretary General's Special Representative for Business and Human Rights, which has been endorsed by business groups, provides a useful tool for companies seeking how to conduct themselves in order to meet the overarching objective of maintaining the social license to operate<sup>1</sup>. The framework stipulates that the state has an obligation to protect human rights, corporations have the responsibility to respect human rights,

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<sup>1</sup> 'Promotion of all Human Rights: Civil, Political, Economic, Social and Cultural Rights, including the Right to Development', Report of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises, UN Doc. A/HRC/11/13 22 Apr., 2009, paras. 50-51.

and people have the right to remedies for rights violations. The respect companies should show is defined as an obligation to exercise due diligence in the form of a 'comprehensive, proactive attempt to uncover human rights risks, actual and potential, over the entire life cycle of a project or business activity, with the aim of avoiding and mitigating those risks'.

## Objectives and Guiding Principles

Considerations such as the above suggest a number of objectives and guiding principles for companies operating in the petroleum and mining sectors. While there is still considerable room for improvement, many extractive companies are fully aware of the principles which follow and have taken steps to implement them.

**Transparency.** Perhaps the most important step companies can take to encourage sound policies and gain the trust of local populations is to be transparent in their own operations and promote transparency and accountability around extraction in the countries where they operate. The principle that the public has a right to full and timely receipt of the information necessary to meaningfully participate in environmental and decision-making has been enshrined in several international instruments, including the Universal Declaration of Human Rights<sup>2</sup>, the Rio Declaration<sup>3</sup>, the Aarhus Convention<sup>4</sup> and the Organization for Economic Cooperation and Development (OECD) Guidelines for Multinational Enterprises. In addition to payments, disclosure of some operational details is required to ensure effective transparency.

**Contract disclosure.** Extractive industry contracts contain information which is critical to public assessment of performance and equity. Withholding this information generates suspicion and can, in many instances, facilitate corruption. Companies should work with government to maximize contract disclosure.

**Extraction decision.** A well-founded decision on whether to proceed with extraction can only be reached through a transparent process and with proper consultation with affected parties, including indigenous peoples, as required by the UN Declaration on the Rights of Indigenous Peoples. The International Council on Mining and Metals (ICMM) Position Statement on indigenous peoples falls short of

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<sup>2</sup> Universal Declaration of Human Rights. UNGA Res. 217A(III), 10th Dec., 1948.

<sup>3</sup> Rio Declaration on Environment and Development, Report of the United Nations Conference on Environment and Development, A/Conf.151/26(VolL), Annex I, 3-14 June, 1992.

<sup>4</sup> Aarhus Convention on Access to Information, Public Participation in Decision-making and Access to Justice in Environmental Matters. Doc. ECE-CEP-43 (25 June, 1998).

this standard, but does accept that ‘following consultation with local people and relevant authorities, a decision may sometimes be made not to proceed with developments or exploration even if this is legally permitted’<sup>5</sup>.

***Open dialogue and engagement.*** In general, an ill-informed public is not conducive to a robust relationship. Public interest is to be encouraged, not feared; engagement of the public in the country of operation in a dialogue about plans for extraction, employment, production methods and other operational details is both just and beneficial to public, government and companies over the long term.

***Minimizing political exposure.*** Companies should not enter into partnerships or contracts with companies owned or controlled by government officials or their families unless their interest is publicly disclosed and legal. International anti-money laundering rules require banks to report transactions with Politically Exposed Persons. In addition, companies should insist that bonuses, royalties, fees and all other payments the company makes to government be made only into properly identified and legitimate government accounts. These accounts and payments should be independently audited—a requirement that should be insisted upon by the companies themselves.

***Internal standards.*** Best practice expectations can be set out and enforced via a clear set of consistent internal standards that staff and sub-contractors are required to follow, backed up by monitoring for compliance and sanctions for breaches. Most major extractive companies have adopted detailed internal codes of conduct<sup>6</sup>.

***Partnerships.*** Companies have the potential to promote positive outcomes for citizens and communities involved in (and affected by) extraction operations. Through partnerships between private actors and government, both local and national, these benefits can be realized, distributed and even multiplied. Local partnerships are especially important as it is at this level that the extractive industries have their maximum direct social and environmental impact<sup>7</sup>.

***Capacity building*** within resource-rich countries is the key to sustained success. As well as training their local staff in best international practice, companies should

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<sup>5</sup> ICMM, Good Practice Guide: Indigenous Peoples and Mining (2011).  
<http://www.icmm.com/document/269>

<sup>6</sup> See, for example, Shell’s Code of Conduct at [www-static.shell.com/static/public/.../code\\_of\\_conduct\\_english.pdf](http://www-static.shell.com/static/public/.../code_of_conduct_english.pdf), and Code of Ethics at [www.shell.com/About Shell/Who we are/Our values](http://www.shell.com/About Shell/Who we are/Our values).

<sup>7</sup> ICMM, Mining Partnerships for Development Toolkit (2011), [www.icmm.com/document/1945](http://www.icmm.com/document/1945)

support capacity building in government and local civil society and encourage governments to seek *pro bono* or paid high quality professional, legal and financial support. A low capacity for government oversight is within the power and interests of extractive companies to remedy. Where auditing capacity is weak, overstretched or non-existent, companies should not take advantage and under-report or manipulate earnings to avoid paying taxes and other payments due.

**Local content.** Local procurement can be encouraged via open competitive processes. Capacity building initiatives will be required in order to improve the competitiveness of local suppliers to international standards. Companies acting in partnership with other stakeholders play an important role in this process (see Precept 10).

**Avoid exceptionalism.** Companies should encourage a level playing field approach in laws and contracts and avoid exceptionalism in host country agreements or stabilization clauses. Seeking special exemptions or taking advantage in gaps in the legal or regulatory apparatus can increase political exposure and prove counterproductive. Exceptions from complying in full with environmental, health and labor regulations should not be sought. In the absence of effective laws, best practice should be followed; in the absence of host country capacity to monitor, audit and enforce agreements, self-regulation is necessary. While company exceptionalism should be discouraged, exceptionalism at the sector level may be desirable.

**Foster best practice.** In addition to implementing best practice training and monitoring, companies should accept a positive obligation to encourage customers, business partners and suppliers of goods and services to adopt similar practices.

## Trade-offs

As with the trade-offs faced by home governments (see Precept 11), extraction companies will also face significant costs in following best practices in some areas. The objectives outlined above all come with costs that can damage the competitiveness of extraction companies in situations where some competitors do not follow the same standards of behaviour.

The objectives of this Precept may benefit extractive companies, particularly in stabilizing the political and economic environment of the resource-rich country. However, these benefits are likely to be long-term and uncertain, in comparison with the shorter-term and more certain costs to a company's competitiveness.

## 2. Instruments and International Initiatives

Extraction companies should seek to adopt, support and otherwise comply with, a range of international initiatives and instruments that can support the dissemination of international best practice and reinforce the efforts by resource-rich countries to improve governance of the extractives sector.

These instruments will also be beneficial for extractive companies, serving to strengthen the operating environment and ultimately improve stability and mitigate against exposure to a range of risks, such as expropriation.

***Extractive Industries Transparency Initiative (EITI)***<sup>8</sup>. Companies should support EITI and report in an open and transparent manner on their activities within each country, so that data from individual countries can be identified. Transparency of revenue streams and other data held by companies is vital to public oversight and key to ensuring that host governments fulfill their duties to citizens. Companies should welcome the level playing field that would be provided by enhancing EITI with a view to making individual company and country-by-country disclosure the standard for participants. Aggregation of all company payments before publication, which is currently the minimum requirement under EITI, reduces the information value of EITI reports to stakeholders, particularly civil society groups, and leaves open the door to possible collusion between governments and companies seeking to mask and divert revenue streams. Many companies already disclose payments to government by major category, making the information more easily accessible to the host country's public, and this should become the common approach. New US legislation (Dodd-Frank Act) requires all listed companies to disclose their payments to governments related to the commercial development of extractive resources, country by country and project by project<sup>9</sup>. The EU may adopt similar requirements.

***Freedom of Information Laws (FOI)***. Companies should adhere to, and support domestic FOI laws in both their home and host countries.

***International guidelines for performance***, such as International Finance Corporation (IFC) performance guidelines<sup>10</sup>, OECD Guidelines on Multinational

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<sup>8</sup> See [eiti.org](http://eiti.org). See also Precept 2

<sup>9</sup> [www.mofo.com/files/Uploads/Images/SummaryDoddFrankAct.pdf](http://www.mofo.com/files/Uploads/Images/SummaryDoddFrankAct.pdf)

<sup>10</sup> [www.ifc.org/performancestandards](http://www.ifc.org/performancestandards)



Corporations<sup>11</sup> (and others), the UN Global Compact<sup>12</sup> and the Global Reporting Initiative<sup>13</sup> are recommended.

***ICMM's Sustainable Development Framework<sup>14</sup>***. The principles of the Sustainable Development Framework developed by the ICMM are a useful guide to beneficial actions and policies that companies can pursue. The framework requires members to work with all stakeholders and integrate sustainable development principles into the planning, operating, designing and closure of operations, as well as implementing prevailing good practice. The latter requires training to ensure adequate competency at all levels within a company, as well as creating a positive obligation to encourage customers, business partners and suppliers of goods and services to adopt comparable principles and practices. Other industry groups would be well advised to formulate similar frameworks.

***Operational transparency***. Extractive companies can report data on production costs, volumes, prices and revenues consistent with proper contract enforcement, using objective standards agreed upon with the host government. Independently verifiable metering of oil and gas is valuable to companies and governments alike, providing a common measurement of production.

***Anti-Corruption Laws***. Companies with operations in OECD countries, which have adopted anti-bribery statutes, risk prosecution if they make improper payments to government officials to secure special treatment or services, even outside the OECD. The US Foreign Corrupt Practices Act is far-reaching and non-US companies have been successfully prosecuted for violating its provisions in third-party countries<sup>15</sup>. Even where the risk of prosecution seems remote, companies should have an absolute ban on corrupt payments. China has adopted an anti-bribery statute.

***Stabilization and host country agreements***. A survey of almost 90 recent host government agreements by the IFC and the UN Special Representative for Business and Human Rights found glaring differences between the terms agreed between entities in OECD countries and the clauses found in agreements between investors and developing countries. Seven of eleven agreements with Sub-Saharan African countries surveyed gave investors blanket exemptions from new social and environmental laws, or obliged the state to pay compensation for the effects of new

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<sup>11</sup> [www.oecd.org/dataoecd/12/21/1903291.pdf](http://www.oecd.org/dataoecd/12/21/1903291.pdf)

<sup>12</sup> [www.unglobalcompact.org/](http://www.unglobalcompact.org/)

<sup>13</sup> [www.globalreporting.org/](http://www.globalreporting.org/)

<sup>14</sup> [www.icmm.com/our-work/sustainable-development-framework](http://www.icmm.com/our-work/sustainable-development-framework)

<sup>15</sup> [www.fcpa.us/](http://www.fcpa.us/)

laws for the duration of the project, regardless of the public interest. Agreements with OECD governments, by contrast, did not offer investors exemption from such new laws or compensation<sup>16</sup>. Companies should voluntarily follow the highest standards and not exploit the weak negotiating capacity of their counterparties.

***Environmental protection.*** Brazil's model oil contract is exemplary in its requirement that 'the concessionaire shall adopt, at its own cost and risk, all the necessary measures for the conservation of reservoirs and other natural resources and for the protection of the air, soil and water in the surface or in the sub-surface, subject to the Brazilian legislation and rules about the environment and, in their absence or lack, adopting the Best Practices of the Oil Industry in this regard'<sup>17</sup>.

Such provisions impose several obligations upon companies (see Precept 5). First and foremost, they must undertake a thorough environmental assessment before commencing operations, prior to which they must agree to steps that will be taken to protect the environment throughout the life of the project and its closure. Thorough mine or well clean up and restoration after closure is of particular concern. Land disturbed or occupied by an operation should be rehabilitated in accordance with appropriate post-extraction uses, with residual wastes and process residues safely stored or disposed of.

No flaring or other egregious contributions to climate change are permitted in the Brazilian model law. The World Bank and Norway have created a Global Gas Flaring Reduction Public Private Partnership (GGFR) which has developed a Voluntary Standard for Global Gas Flaring and Venting Reduction to minimize continuous flaring and venting of associated gas<sup>18</sup>. The Standard includes monitoring and transparency guidelines, best practice, and a timeline for implementation. Preventing other noxious releases, such as oil spills and the leak of toxic chemicals,

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<sup>16</sup> Stabilization Clauses and Human Rights, a research project conducted for the IFC and the United Nations Special Representative to the Secretary General on Business and Human Rights [http://www.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/p\\_StabilizationClausesandHumanRights/\\$FILE/Stabilization+Paper.pdf](http://www.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/p_StabilizationClausesandHumanRights/$FILE/Stabilization+Paper.pdf)

<sup>17</sup> Concession Agreement for the Exploration, Development and Production of Oil and Natural Gas. Federal Republic of Brazil, Ministry of Mines and Energy, Agencia Nacional de Petroleo, Gas Natural e Biocombustiveis (2008), Clause 21.1.

<sup>18</sup> The partnership currently includes the World Bank; major oil producing nations such as Angola, Cameroon, Canada, Chad, Ecuador, Equatorial Guinea, Indonesia, Kazakhstan, Nigeria, Norway and the United States; and major oil companies including BP, ChevronTexaco, ENL ExxonMobil, Marathon, Norsk Hydro, Statoil, Shell, TOTAL and Sonatrach.

<http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTOGMC/EXTGGFR/0,,menuPK:578075~pagePK:64168427~piPK:64168435~theSitePK:578069,00.html>

such as mercury, into the environment is obligatory under best practice and the ICMM has specific guidelines for its members regarding the use of mercury in mining.

***Protecting the safety and welfare of workers.*** International labor standards are provided by the International Labor Organization's (ILO) Core Labor Rights and the Tripartite Declaration of Principles Concerning Multinational Enterprises & Social Policy, both of which are also incorporated in the United Nations Norms on the Responsibilities of Transnational Corporations and Other Businesses Enterprises with Regard to Human Rights<sup>19</sup>.

***Accounting for local Impacts.*** Extractive operations often lead to displacement of local populations or disruption of their livelihoods. Agreements can be negotiated with individual property holders, but communal lands present special challenges. International law recognizes that indigenous people have inherent rights derived from distinct ethnic and cultural identities and their close and special attachment to their ancestral lands, which may be managed communally. The UN Declaration on the Rights of Indigenous People confirms their right to just and fair compensation for the use of their land, knowledge and resources. The Mining, Minerals and Sustainable Development (MMSD) initiative calls for benefit-sharing arrangements that go beyond fair compensation for damages to ensure that indigenous people benefit<sup>20</sup>. Company obligations to respect indigenous rights remain even where the host government fails to do so, and it remains in the interests of companies to reduce the risk of costly disruptions, litigation and damage to reputation.

Above all, company interests and local rights are best served via thorough consultation based on access to full information. ICMM Principle 4 requires that members 'consult with interested and affected parties in the identification, assessment and management of all significant social, health, safety, environmental and economic impacts associated with our activities'. As part of the mandatory

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<sup>19</sup> Freedom of Association and Protection of the Right to Organize Convention, ILO Convention No. 87 (1948); Right to Organize and Collective Bargaining Convention, ILO Convention No. 98 (1949); Forced Labor Convention, ILO Convention No. 29 (1930); Abolition of Forced Labour Convention, ILO Convention No. 105 (1957); Minimum Age Convention, ILO Convention No. 138 (1973); Worst Forms of Child Labour Convention, ILO Convention No. 182 (1999); Discrimination (Employment and Occupation) Convention, ILO Convention No. 111(1958); Equal Remuneration Convention, ILO Convention No. 100 (!951); ILO Tripartite Declaration of Principles Concerning Multinational Enterprises & Social Policy (Nov., 1977).

<sup>20</sup> International Institute for Environment and Development, Finding Common Ground: Indigenous Peoples and Their Association with the Mining Sector. (2003). [pubs.iied.org/pubs/pdfs/9267IIED.pdf](http://pubs.iied.org/pubs/pdfs/9267IIED.pdf)



regular review and updating of risk management systems required of adherents to the ICMM Principles, members must inform potentially affected parties of significant risks from mining, minerals and metals operations and the measures taken and pending which will manage these risks.

Consultation alone is insufficient, however. Where appropriate, compensation may take the form of possibly sharing in the earnings of extraction, as Exxon has offered in the Cepu Block in Indonesia, where local governments have an equity share in production. Training and employment opportunities can be offered in fields related to the extractive activity alongside a supportive stance towards government efforts to increase local content and value-added. Such support can be expressed further by procuring services and products locally to the greatest extent possible and investing in downstream operations in the country of extraction where commercially feasible and consistent with government policy (it may be that the country's economic diversification objectives would prioritize investments outside the sectors; companies should respect these objectives).

***Public services and infrastructure.*** In the absence of state-provided healthcare, housing, infrastructure and education, nations may look to extractive companies to provide these services as a condition for winning a concession. Alternatively, government may offer to pay for large scale infrastructure with future oil or mining proceeds. There is nothing inherently wrong with such arrangements. However, they may result in confusion about where the ultimate responsibility for providing public services lies. The track record of package deals in delivering the stipulated part of the 'package' is also decidedly mixed. Governments have the duty to protect and provide for their citizens; companies have the responsibility to respect government policies. If governments and companies agree that a company is better placed to provide services, companies can fulfill such commitments and governments must monitor and audit company services. Companies can protect themselves against charges of failing to deliver if they make public the individual elements of such packages and publicly disclose financial terms and services to be provided (as well as the timeline for delivery).

### **3. Implementation**

***Cultivating a culture of Best Practice.*** Endorsing international norms and best practice is not sufficient; effective management systems are crucial. Extractive companies are complex structures with multinational, multicultural employees operating in far-flung and remote regions. Senior management needs to exercise



special diligence in embedding international norms and industry best practices throughout the corporate structure and extractive operations.

Cultivating a culture of best practice begins at the top with clear policies endorsed by the Board of Directors, whose policy guidelines should be disseminated widely and publicly as part of a campaign of instilling values and policies in the corporate culture and throughout the company's management systems—and, to a more limited extent, beyond. This will require systems for tracking performance and expeditious action to correct deviations.

Local managers, in particular, have an important role to play in keeping a door open to civil society, especially in regions of operation, in order to catch problems early. Senior international management has a responsibility to insist that local representatives fulfill this role. In addition, the proliferation of higher standards should not be limited to the company's management structure; so far as possible, companies should try to ensure that suppliers and service providers meet the same standards.

The ICMM Principles have been promulgated by the CEOs of the member mining companies, signaling the high level commitment necessary for replacing a race to the bottom with a concerted raising of standards. The ICMM also requires that companies offer independent verification of compliance with their principles. This approach should be more widely adopted. ICMM-type principles could be developed for the petroleum industry, while all extractives should pursue contract transparency as the industry norm.

Through such industry groups and other means, other extractive companies can be brought into a concerted effort to mainstream and universalize best economic, environmental and social standards for extraction. State companies and emerging market enterprises in particular should be engaged, since they play an increasingly important role in the international extractive industry. Strong international accounting standards will greatly facilitate the mainstreaming of rising standards and should be supported and expanded to include country-by-country and project by project reporting of reserves and production, as well as costs and payments.

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