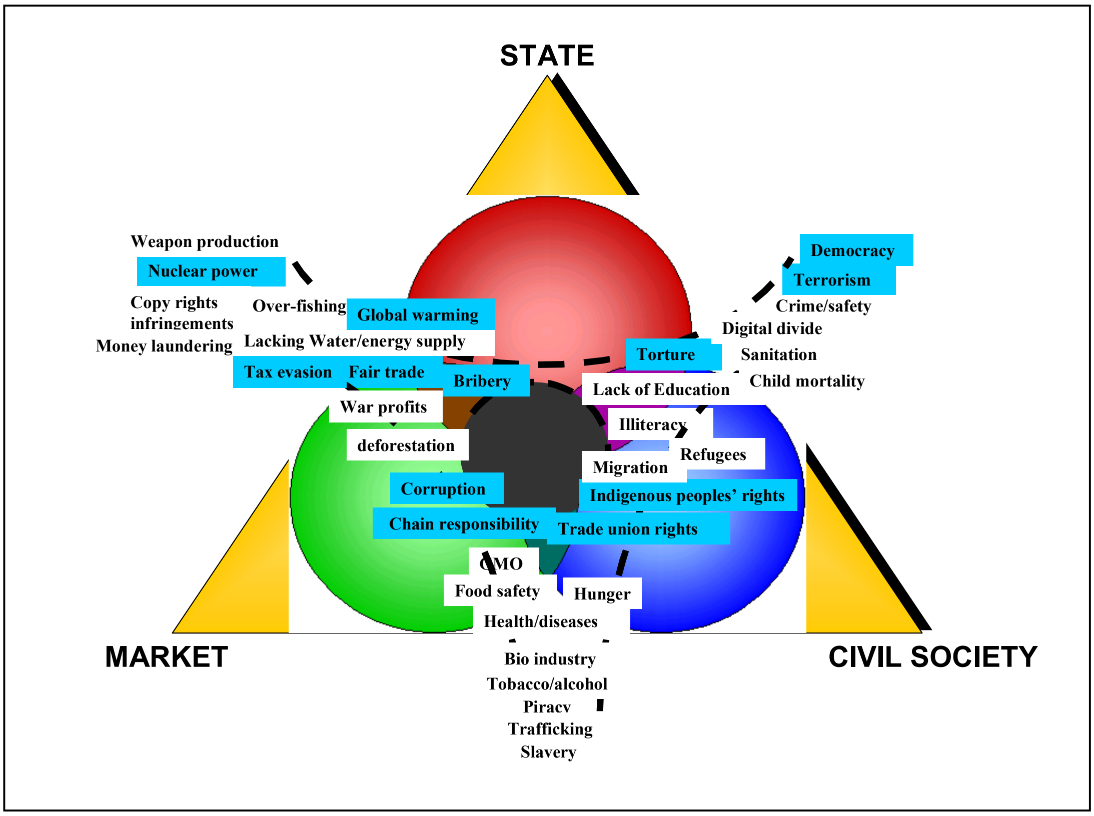
SUSTAINABILITY CHALLENGE # 1:
FAIR ACCESS TO RESOURCES

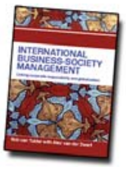
Key Interface issues for resources industries


STATE
MARKET
CIVIL SOCIETY
Weapon production
Nuclear power
Copy rights infringements
Money laundering
Over-fishing
Global warming
Lacking Water/energy supply
Tax evasion
Fair trade
Bribery
War profits
deforestation
Corruption
Chain responsibility
Trade union rights
GMO
Food safety
Hunger
Health/diseases
Bio industry
Tobacco/alcohol
Piracy
Trafficking
Slavery
Democracy
Terrorism
Crime/safety
Digital divide
Sanitation
Child mortality
Torture
Lack of Education
Illiteracy
Refugees
Migration
Indigenous peoples' rights

1. Introduction: on resources, strategic industries and a sustainable corporate story[1]

The industry that is confronted with the largest number of interrelated interface issues, is arguably the extractive industry - in particular the petroleum/oil industry. This industry can therefore be used as a first and more elaborate example for identifying the general components of a sustainable corporate story. Major issues for the oil industry develop

[1] This issue dossier was written by Rob van Tulder. It elaborates one theme that has been addressed in chapter 10 of the book (on 'The Stakes – Firms part of the problem or part of the Solution'). References in the text to Figures, Chapters and Tables, refer to the original book "International Business-Society Management" (Van Tulder with Van der Zwart, 2006). The dossier is intended to illustrate how this particular issue can be approached by both scientists and practitioners. Last updated: March 2006.



along all societal interfaces, but especially along the public-private interface where governments and business meet: corruption, fair trade, bribery, tax evasion, energy supply, pollution and global warming. Can resources firms be considered part of the problem, part of the solution or both?

Other industries that can be classified as 'strategic' like electronics, automotive or agriculture are faced with comparable interface challenges. Oil, however, is the most strategic resource in the world. It provides the energy input for most other industries and is at the basis of a large number of vital products such as plastics and new materials. Oil reserves are very unevenly distributed over the world and therefore represent a classic motive for internationalisation: resources-seeking. Profit margins are high, but governments also impose high levies for strategic reasons. The disposition over oil creates the natural boundaries of the growth models for most economies. The rivalry between all five economic models in the world (liberal, corporatist, business-statist, religious-autocratic and community) is strongly affected by their disposition over oil and natural resources.[2] Lack of energy is among the key forces preventing economic and social development, and slowing down poverty reduction and growth of the rural sector (Worldbank, 2002).[3] When the Chinese economy started to grow, its first worry has been to safeguard access to sufficient oil reserves – just as oil-poor Japan had to do three decades earlier.[4]

Intensification of redistribution battles

Some of the biggest international armed conflicts in the 15 years since the fall of the Berlin Wall like the Gulf War were strongly connected to safeguarding access to oil reserves and other natural resources.[5] The increasing number of countries in the 1990s (chapter 5) created also an increasing number of stakeholders in decision-making processes over transport lines for oil and gas. It gave rise to a new type of diplomacy: pipeline-diplomacy.[6] Resources companies are directly or indirectly, but in any case regularly, involved in civil and interstate wars. A UN Panel of Experts in 2002, for instance, concluded that at least 85 international companies were illegally exploiting natural resources in the war-struck Democratic Republic of Congo (Wortel, 2004). There is no international consensus, however, on the exact responsibilities of firms in conflict areas.

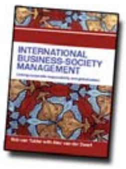
[2] The fate of the two contending models identified in chapter 2 (religious-autocratic and community) is perhaps even stronger – and often negatively - attached to the natural resources sector than the fate of the three most successful rivals. The economic and political position of the religious-autocratic regimes in the Middle-East is almost completely based on their posession of the largest oil reserves in the world; the communities of indigenous peoples clash with international resources companies due to the presence of natural resources (mining, forest) in their natural habitat.

[3] The number of people without access to modern energy services to meet basic human needs and economic development is assessed at around 2 billion people – an increase compared to the 1970s (Worldbank, 2002).

[4] The better bargaining skills of Chinese diplomats as opposed to diplomats of India in closing contract on the access to oil deliveries is suggested to have been a major factor in explaining the better growth possibilities of China vis a vis India.

[5] In 2001 about a quarter of the around fifty wars and armed conflicts in the world revolved around resources such as diamonds, coltan, oil, timber and gold (Renner, 2002).

[6] Sometimes rephrased by idealists as *peacepipe*-line diplomacy.



With the proven reserves of oil and other natural resources reaching their limits, redistribution conflicts over resources are bound to increase in the future. Oil and resources companies have to operate in countries with the most corrupt and oppressive regimes. Many firms present this as a fact of life – as an environmental factor that cannot be changed – for which a good political risk analysis is the most appropriate tool (see chapter 13). But this underestimates their actual involvement in this mechanism. The presence of big resources companies in relatively poor countries almost always leads to distributional fights among local groups and breeds kleptocracy[7], poor governance and the breach of basic human rights involving denial of trade union rights, torture, or lacking democracy. Human rights issues accidents are strongly associated with the international operations of oil firms (see, e.g., Haller et al., 2000; Tomei, 1998).

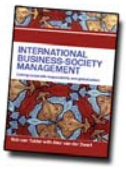
Natural resources firms are therefore always confronted with the tactical question whether or not they should engage in bribery or illegal commissions. The stance towards bribery also depends on the degree to which the national home government is prepared to indulge on the praxis of bribery.[8] Most western European and North-American governments have implemented sanctions on firms engaging in bribery. Statoil of Norway paid a fine for bribery in Iran, the American company Halliburton had to withdraw from Nigeria due to corruption. On the other hand, in France, until recently the payment of illegal commissions in other countries was tax deductable (Volkskrant 17 January 2004).

Doing business in oil - as in many other natural resoures - makes it extremely difficult to separate business from politics. Daniel Yergin (1991), who won a Pullitzer price for his chronic of the petroleum industry, characterizes oil as 90% politics and 10% business. Home governments are actively involved in the negotiations over oil contract. They are regularly asked to intervene in support of exploration and extraction contracts for their national champions.[9] This further strengthens distributional conflicts, because natural resources contracts are usually aimed at exclusivity, which makes the bargaining process part of a zero-sum game (what one wins, the other loses) transforming the public good into a private or club good. Due to their oligopolistic nature and their position as a

[7] In the Global Corruption Report 2004, Transparency International notes that corrupt government leaders were in the past supported by western state donors. For various reasons, the Presidents Suharto of Indonesia, Marcos of the Philippines and Mobutu of Zaire are assessed to have obtained together more than 50 billion dollars – more than the whole annual volume of western development aid. Corrupt leaders continue to exist. But the origin of the financial support for corrupt leaders has moved from governments to companies, according to Transparency International. The list is headed by firms from Australia, Sweden, Switzerland and Austria. The arms and oil sector figure prominently in the supply of funding for corrupt officials.

[8] Bribery is primarily addressed as a problem by North-American and European governments: Parmalat and Telefonica, City Bank and IBM got convicted for bribing government officials in Latin America. This might give the falls impression that only these firms are involved in paying bribes in developing countries. Firms stemming from other institutional models have a different conception of bribery and therefore tackle this issue differently.

[9] In the 2004 global Corruption report, John Bray (2004: 317) signals the general perception that firms from OECD countries gain business advantage because of political pressure from their own governments. Only around eight percent of the respondents in a 2002 survey amongst managers – all senior officials at or near board level – stated that government pressure had never played a role in gaining business advantage in their foreign affairs.



strategic industry in most countries, the oil industry in particular is regularly suspected of collusive behaviour – often by stakeholders in host countries.

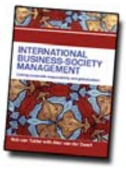
Furthermore, oil and the petro-chemical industry is deemed synonymous with pollution. So it is held at least partially responsible for a number of the ecological problems in the world. Oil spills related to oil majors and the disputed disposal of oil production sites have been prime triggering events for NGOs to put the environment on the agenda (Table 9.2). In these cases the primary responsibilities of companies can directly be addressed. But the extensive and systematic *use* of oil products creates much bigger and structural ecological problems, which are situated at the societal interfaces and is not the prime responsibility of the oil companies themselves. In case citizens are not prepared to pay higher airfares – to include energy costs –, make less use of cars – to reduced petrol consumption – or use less energy in their houses, ecological problems are bound to endure.

Finally, trade in oil and natural resources can be considered neither 'fair' nor 'free'. Prices in oil are set in an intricate interaction of OPEC countries tactics, subsidized production in other localities, price formation on a limited number of 'spot markets' and always strongly influenced by tax regimes and the decisions of governments on sustaining strategic oil reserves. Comparable conditions apply to the trade and price mechanism in other natural resources. Natural resources and agricultural products share extremely 'uneven trade' conditions which has resulted in more volatile and poorer trade income for those at the bottom of the international supply chain.

2. A sustainable corporate story for the extractive industries?

The challenges faced by multinational resources companies in creating a sustainable corporate story, provide a good example of the complexities in dealing with interrelated interface issues. A sustainable corporate story involves both strategic and operational choices. The *strategic focus* of firms and the industry is at stake: should firms try to diversify away from their original industry in order to prevent ecological issues from appearing? All oil companies have considered this option, none has been able to really implement this strategy - partly because of the sunk cost involved in their present business, partly because of pressure by the societies that consume large quantities of oil. Oil companies can make their business more sustainable, though, by developing clear and integrated visions on how to achieve ecological sustainable growth and using their sizable financial means in developing real alternatives to the energy and mobility needs of mankind. The bargaining dynamics applies here as well: being first not necessarily reaps longer term profits, whereas a wait-and-see or free-rider strategy can be very profitable in the short run.

A credible and realistic sustainable corporate story should take the industry dynamics into account and the roles that individual firms can or should adopt. This can be dubbed the problem of conditional morality (see box). The dynamics of the industry involves a credible story on the roles needed of other actors such as governments and civil society stakeholders. The powerful position of oil companies in most countries and in international supply chains raises special responsibilities. This is further supported by international organisations and NGO that plea for a bigger commitment of corporations to solving international issues. UN Global Compact and consultancy SustainAbility for instance claim that corporate responsibility for markets alone is an inadequate response to



mounting problems such as climate change and HIV/Aids. They called for more corporate engagement in political decision-making (Ethical corporation, 31 July 2004). The statement, however, underestimates the degree to which companies like oil majors are already engaged in political circuits.

Conditional morality or how to evade becoming the 'sucker':
MNCs and their relative position towards international issues

Basu (2001) and Streeten (2001) have considered the various roles multinationals can take in addressing international Corporate Reponsibility (ICR) issues such as poverty alleviation, child labour, environmental issues, war, corruption. Four roles can be distinguished:

(1)an MNC can choose not to be actively involved in addressing the issue, while others are; this is comparable to a 'free-rider' situation, in which the MNC hopes the others will either solve the problem, or the non-participation will not lead to reputational damage;

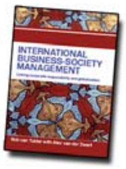
(2)the MNC becomes active on the issue but only if other MNCs do the same; this option relates to Basu's concept of *conditional morality* (see also chapter 11);

(3)no MNC is involved in the issue or only pays lip-service to the issue; this is comparable to a 'prisoner's dilemma' situation where all actors wait to take an initiative or take sup-optimal action;

(4)an MNC is the only company active on the issue; the firm is acting according to the so-called categorical imperative, but in the view of Streeten (2001) runs the risk of being a '*sucker'*;

In situations 1 and 3, the individual MNC plays no role in addressing the issue, while it will in 2 and 4. If each behaves according to 1 or the fear of 4 (not wanting to be 'the sucker'), this leads, on conventional assumptions, to outcome 3. Although 2 is preferred to 3, we end up with the less preferred situation 3 unless rewards, penalties, autonomous cooperative motivations, or behavior according to Basu's conditional morality leads to 2. It must be noted that MNCs will not necessarily behave according to these assumptions – there are intrinsic and extrinsic factors, including societal norms and expectations, that drive CSR behavior.

The biggest sustainability challenges resources firms face is in their relationships with central governments and local communities. Firms can decide to retreat to their home turf in order to lower the number of potentially controversial issues with host governments (like corruption and human rights issues), but this deprives them and their home countries from control over strategic inputs and is therefore unrealistic. Business leaders have to consider whether they apply a strategy in which they adapt to local cultures and customs or whether they want to create a universally applicable strategy and ethics (chapter 13). Oil firms very often are very big compared to local governments in developing countries. This gives them a very strong bargaining position, but also additional responsibilities in addressing any issue that might mature in the host country. Shell for instance developed a 'primer on child labour' even when the issue does not affect them directly (no children work in oil drilling). In case firms retreat to their home base in order to make it potentially simpler to create a sustainable story, they should realise that the nature, not



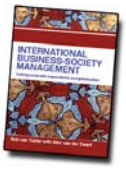
necessarily the magnitude, of their problem alters: from direct responsibility over production to responsibility over international sourcing and supply chains.

Operational challenges in designing a sustainable story

A large number of *operational features* of resources firms are at stake as well: how to modify the negative consequences and/or enhance the positive consequences of acts. A sustainable corporate story almost always involves trade-offs that have negative effects for particular actors. Win-win situations are difficult to achieve in the short run (see chapter 6). By investing in (end-of-pipeline) technologies to reduce emissions and pollution, oil companies can make their business more acceptable to society. By developing a number of rules (codes) firms can engage in self-disciplining measures that for instance lower the change that they stimulate corruption and bad governance. Multinational Enterprises (MNEs) are considered by many to have a special duty in reducing corruption. If MNEs adopt a policy of not bribing 'they would have removed one of the two parties: the party (MNEs) willing and able to corrupt, leaving the other party (host country politicians and bureaucrats) willing to be corrupted without the needed accomplice" (Iyanda, 2004: 9). Donaldson (1989; chapter 11) even notices that anti-corruption policies can act as a 'competitive advantage' for these firms. MNE companies can identify with civil society groups in their struggle against oppressive regimes and bad governance. But this option is particularly difficult to implement given the fact that oil is more about politics than about business.[10]

Another operational venue that is particularly relevant for the extractive industries, is to create greater transparency as regards financial transfers from governments to firms (subsidies, tax holidays) and vice-versa (tax payments). Corruption is enhanced by secrecy and poverty is prolonged if governments are not capable (or willing) to use tax income for investment in their economies. So, an initiative to create greater transparency in this area could create a more sustainable tax foundations for developing countries, which increases the change of poverty alleviation (through lower corruption) and which is in the longer term interests of the extractive companies themselves as well (see box). Transparency on tax payments is not an easy aim, but can be considered to present a more convincing corporate story than a plea for transparency in general, without efforts to address really major issues.

[10] "the many court cases pending against several MNEs for their role in Nigeria, Burma, South-Africa, Sudan (…) suggest that MNEs tend to support oppressive regimes, rather than the civil society in such struggles." (Iyanda, 2004:10)



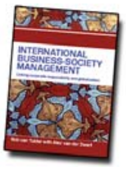
“Publish What You Pay” and the Extractive Industries Transparency Initiative

The “Publish What You Pay” campaign (PWYP) is backed by a worldwide coalition of over 170 non-governmental and civil society organisations. It was founded by Global Witness, George Soros' Open Society Institute, CAFOD, Oxfam, Save the Children UK, and Transparency International UK, to advocate that mineral revenue transparency is a fundamental governance issue and that voluntary efforts by extractive industries (oil, gas, mining) to address the problem had failed. Revenues from extractive companies (taxes, royalties, signature bonuses) should be an important engine for economic and social development in developing and transition countries. The lack of accountability and transparency in these revenues can exacerbate poor governance and lead to corruption, conflict and poverty. Sources within the World Bank, IMF and elsewhere confirm the magnitude of resource revenue misappropriation in developing mineral-dependent countries. It is, for instance, suggested that at least US$1 billion of the Angolan government’s oil receipts have remained unaccounted every year in the 1998-2003 period. In Equatorial Guinea, the entire government income from oil – about US$135 million, which is 90% of the country’s foreign export earnings – may be disbursed offshore and remains unaccounted for in the state budget. At least US$4 billion of Nigerian government funds – some 90% of which came from oil – were stolen by General Abacha during his dictatorship. In order to empower citizens and institutions in developing countries to hold their government to account, transnational extractive companies should reveal the same basic information about net payments to the state that they already routinely disclose in the developed world. The PWYP-coalition calls for mandatory disclosure requirements, either as a stock-market listing rule or as an International Accounting Standard (IAS).

At the World Summit on Sustainable Development in Johannesburg in September 2002, UK Prime Minister Blair embraced the issue as well and initiated – in close consultation with NGOs like Global Witness, investors and some firms – the Extractive Industries Transparency Initiative (EITI). The aim is to increase transparency over payments by companies to governments and government-linked entities, as well as over host country government revenues. In the words of Blair: “Good governance and transparency serve the interests of the business community, wherever it operates. Better openness and accountability are essential to securing the stability and prosperity that the developing world needs, and on which our mutual business success depends.” (Financial Times, 29 September 2003). The way to achieve increased openness is a process of intense multi-stakeholder dialogue and of building broad consensus between all parties involved: G8-members, governments of developed and developing mineral countries, NEPAD, UNDP, The World Bank Group, extractive companies (transnational, as well as state-owned), contractors, trade associations, NGOs and civil society organisations.

In both campaigns, it is acknowledged that any transparency option needs to address three key dimensions – in order to engage both the extractive corporations and governments:

- **Legality**: in countries where companies are subject to a non-disclosure clause or agreement, or a law on public disclosure, the transparency option must ensure that the company has received whatever consents are necessary prior to disclosure. To illustrate the relevance: When BP wanted to publish its tax payments to the Angolan government in 2001, its local business partner Sonangol (the national oil company) immediately threatened with termination of BP’s concession, and BP recoiled from implementing its intentions.
- **Competitiveness**: the disclosure of data on country-specific payments should not put



companies at a competitive disadvantage. A level playing field must be ensured. Companies have opted for a ‘clearing house’ construction, which facilitates collection and synthesis of revenue data without laying bare confidential commercial information. The World Bank and the IMF could function as ‘honest brokers’ and aggregate the data from governments and companies before dissemination.

- **Alignment**: the pursuit of transparency must be carried out by companies and host governments in parallel, applying to – for instance – monitoring, auditing and publication of data.

Sources: www.publishwhatyoupay.org ; www.eitransparency.org

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