
Photo: Jerry Galea/OxfamAUS

THE UNIVERSITY OF MELBOURNE

MELBOURNE BUSINESS SCHOOL

Mt Eliza

EXECUTIVE EDUCATION

ASIA PACIFIC SOCIAL IMPACT LEADERSHIP CENTRE

Melbourne Business School

Creating social impact through collaboration.

Sustainable mining — managing corruption risks and revenue transparency


Photo: Natasha Newman/OxfamAUS

COMMUNIQUÉ, JUNE 2012

Introduction

Oxfam Australia and the Melbourne Business School (Asia Pacific Social Impact Leadership Centre) partnered to host the third annual Sustainable Mining Symposium. The symposium was held in May 2012. This year, the focus was on managing corruption risks and revenue transparency in the extractives sector. The event was held under Chatham House rules.

The symposium provided information and stimulated discussion on global developments in the following areas:

- the fight against corruption
- the high risks for the extractives sector, particularly through third party relationships
- industry responses to corruption
- Australian Government anti-corruption and revenue ransparency activities

Topics discussed included the Extractive Industry Transparency Initiative (EITI) and compliance and enforcement with anti-corruption legislation. The symposium participants also discussed the challenges mining companies face at "ground level", the investors' perspective, and the impact corruption has on communities — and particularly on women — in developing countries. Participants also discussed the relationship between poor governance and corruption, thus highlighting the complexity of the issue.

Participants included representatives from mining, oil and gas companies, industry associations, financial institutions and auditor and legal firms. The symposium was also well attended by Australian Government representatives, academia and civil society.

The opening session set the scene. The Melbourne Business School made it clear that no enterprise is immune to corruption risks, and the harm caused to an organisation's financial position, reputation and constituents is significant. Nonetheless, managing those risks is not simple. Different cultural, personal and ethical interpretations of corruption are often cited as a defence. With this in mind, the best company response is a zero tolerance policy.

Oxfam Australia's position is that minimising the risk of corruption, as well as disclosing extractive industry revenue flows, is a critical factor in promoting sustainable mining. It will help ensure communities get a fair share of their natural resource wealth and assist in holding both governments and companies to account for the management of the industry and distribution of benefits.

Background

In the wake of the global financial crisis, 2012 may well be remembered as the year that corruption, transparency and accountability became a uniting call in rich and poor countries alike.

There is global recognition that the extractives sector is heavily exposed

OXFAM Australia

to corruption risks. The Transparency International Bribe Payers Index 2011[1] confirms that the mining sector is perceived to be the most likely to pay bribes, after oil and gas, real estate, utilities and public works and construction.

This results from their growing business activity in resource-rich, corruption-prone countries and their reliance on intermediaries and extensive supply chain relationships. Participants heard that "there is a depressing correlation between corruption and natural resource wealth". Extractives are a high risk, high return endeavour, but the benefits are not always equitably shared or used for essential services. Corruption is the most pervasive risk for the sector.

Global anti-corruption regulatory frameworks continue to be strengthened and are becoming more coherent. These include:

- Organisation for Economic Co-operation and Development (OECD) Convention on Combating Bribery of Foreign Public Officials in International Business Transactions
- Australian Criminal Code Act
- United Kingdom Bribery Act
- United States Foreign Corrupt Practices Act

Additional global developments confirm the mounting pressure to fight corruption and ensure the global resource boom benefits all. These include the Wall Street Reform Act (also known as the Dodd-Frank Act 2010) — which will require all oil, gas and mining companies listed on the US Securities Exchange to disclose payments made to foreign governments — similar European proposals and the EITI pilot in Australia.

Why transparency matters

The moral argument for transparency is clear: natural resources belong to the people and governments have a responsibility to ensure the people benefit from resource extraction. Symposium participants were told that the power of transparency is its ability to make life better for people. The role of activists, journalists, non-government organisations and citizens is crucial, and these groups should be supported to demand accountability from their governments.

Transparency means corruption is more likely to be identified in its early stages. It increases trust among stakeholders, assists communities in holding their own government to account, encourages governments to perform better and to strengthen their own regulatory frameworks.

Corruption is not good for business. It can fuel conflict, disrupt production, have an impact on competitiveness, tarnish reputation, jeopardise investor confidence and erode the "social licence" to operate. Corrupt governments are often unstable and this poses additional business and community risks. Participants heard that transparency does pose an additional cost to business but that "transparency should never be seen as a burden, any additional costs to business are relatively small, an estimated 0.05% of gross revenues."

Participants expressed the view that strong anti-corruption legislation in more countries improves the chance of companies seeking to implement best practice. Without the necessary legal framework, the conversation cannot even begin. It was also said that companies can work transparently in corrupt environments. It was suggested that state-owned enterprises, such as some in China, are most likely to respond to global demands for greater transparency.

Regulation, compliance and enforcement

The G20 anti-corruption agenda and strengthened engagement with the OECD has resulted in a number of countries, including Australia, reviewing their anti-corruption legislation. In the Australian context, the government is considering removing the "facilitation payment defence" from the Criminal Code. Facilitation payments are not harmless — they have a corrosive effect on sustainable economic development and the rule of law. Regardless of the decision by the Australian Government on this matter, the point was made that facilitation payments may be illegal in the country in which they are paid, and they are prohibited under UK law. Hence, the risks are just not worth it.

Participants learnt about the components of an effective anti-corruption policy and compliance program. Such a program should include efforts to:

- understand the operating context where business is being done
- document the risks and undertake a gap analysis, including the efforts that have been undertaken to manage identified risks
- develop codes of conduct and policies that prohibit bribery and define money laundering. This should include an explanation of what employees can and cannot do, and what improper conduct and contributions are considered to be
- deliver training to staff so they understand company policy
- manage third party risks to ensure they understand their obligations and the importance of due diligence
- establish a compliance mechanism to monitor implementation

It was suggested that a "top-down" commitment to anti-corruption is needed. Interventions from symposium participants confirmed that the real challenge is to move beyond board room commitments to developing anti-corruption policies that work at ground level. Additional complexities were raised. In an era when mining companies are expected to stimulate the local economy, compliance with anti-corruption policies along business supply chains may "knock out local suppliers".

[1] Transparency International, "Bribe Payers Index 2011"

Participants heard that while corruption can start from small misdemeanours and misconduct, at its worst it may involve huge sums of money and implicate high levels of government. In this context the Australian Federal Police take their role of investigating corruption allegations seriously.

The Extractive Industry Transparency Initiative in Australia

In 2011, the Australian Government announced efforts to improve revenue transparency in the extractives sector in Australia through the establishment of an Australia EITI pilot. While some believe there is already a high level of transparency in Australia, this will be tested through the pilot process. It was noted that the EITI has the support of the United Nations, G20, G8, the African Union and European Union.

The EITI pilot will operate in accordance with the globally-established EITI rules and principles. It will identify costs and benefits, gaps in existing revenue reporting systems and lessons for the international arena, particularly for other OECD countries. A multi-stakeholder group of industry, government and civil society representatives has been established to oversee the pilot and make recommendations to the Australian Government on the full implementation of the EITI.

In addition to piloting the EITI, Australia is making a $12.7 million contribution to the EITI Secretariat over four years to assist in promoting the EITI and to support other countries in implementing the initiative.

Similarly, the United States has recognised the need for a broader effort in improving governance in the extractives sector. Corruption and limited accountability for management of the extractives sector is not seen as just a developing country's problem — as demonstrated by the financial crisis, Deepwater Horizon and corrupt behaviour between some officials and oil companies. The United States recently announced that it will implement the EITI and an EITI multi-stakeholder group is expected to be in place shortly. Like Australia, the US landscape is complex due to state jurisdictions as well as tribal rights and interests.

The point was made that while EITI can improve transparency, the real challenges lie beyond revenue disclosure. For example in some countries, much of the mining sector is funded by "dubious sources" and it is necessary to have complementary transparency in the banking and financial sector regarding the funding of projects.

The miners' perspective: understanding challenges and company responses

The symposium participants heard that there are companies who have strong integrity and compliance programs which are most effective when supported by a strong corporate culture of "speaking up". This was summarised as "tone at the top" and "tone in the middle", meaning that company chief executive officers and operations managers must clearly state and regularly reinforce company expectations and policies regarding corruption.

For most companies, combating corruption is a steep learning curve. Smaller companies are often "feeling their way" forward, while larger companies may be keener to adopt a more systematic approach due to several recent high-profile cases.

Doing business in challenging jurisdictions (including countries experiencing social chaos or civil war) and supporting employees to manage corruption risks is very difficult. In some countries, culturally entrenched patronage systems and "big man" politics are additional challenges. This can result in community mistrust of government and industry relationships. In these contexts, legal solutions alone are not going to combat corruption. There is an urgent need to better understand the cause and effect of poor governance and corrupt practice. There is no single answer, but there were suggestions that the multi-stakeholder dialogue process at the heart of the EITI could help.

Participants heard examples of Australian companies that are disclosing information on the payments they make to host governments. They also heard about Australian companies providing assistance to host governments to strengthen relevant institutions such as mining departments, and disclosing the details of financial support for community projects. However, push-back from the local company and manager can be an issue, with some claiming they need to "make payments to get ahead". It remains a challenge for companies to have a compliance policy that improves operations on the ground.

Participants heard that most corruption prosecutions involve third parties. It was suggested that the construction phase, when large numbers of contractors are involved, is most risky because it's easy to lose control. It became apparent that what's needed is greater due diligence of business partners and more assessment of corruption risks linked to contractors and suppliers. It was noted that the updated OECD Guidelines for Multinational Enterprises have strengthened provisions regarding due diligence and responsibility for business relationships.

An additional area of exposure was through the payment of funds for community projects. Participants heard that "corruption happens with two siblings: collusion and nepotism". How funds for community projects are spent is crucial to a company's ongoing social licence to operate. One approach discussed was trying to involve local communities in deciding how the money should be spent.

An investor's perspective on Australian company responses to bribery and corruption

One "bittersweet" outcome of the global financial crisis is the increased global attention on corruption and transparency. Financiers are increasingly aware that corruption and bribery risks can quickly become financial risks for investors. Corruption costs $1.5 trillion globally, and is a pervasive obstacle to the long-term value of companies. This can remain hidden for years and, when exposed, leads to a massive devaluation of an investment, with shareholders bearing the cost and communities bearing the impact.

A recent report on the exposure of Australian companies to corruption and bribery risk[2] indicates that ASX-listed companies lag behind the rest of the world in terms of managing bribery risks. Those companies with inadequate policies have "raised a red flag" for investors, who are keen to understand and minimise risks related to bribery and corruption, including along the supply chain. Similarly, shareholders are becoming increasingly vocal and are demanding more rigorous due diligence.

Other research[3] discussed at the symposium showed that the extractives sector faces particular challenges because their operations are often located in high-risk jurisdictions and because of their reliance on intermediaries.

Participants were advised that the United States is directing its attention to relationships between companies and third parties. Companies can no longer afford to **not** "look under the rock", no matter how painful that may be. It confirms the need for robust due diligence before entering into business relationships. Companies need a process for measuring risks and procedures that will stand up to scrutiny.

Some investors believe that ASIC requires a greater regulatory role. Furthermore, some investors support payment disclosure legislation (rather than securities exchange listing rules) and the implementation of EITI in Australia.

Corruption and revenue transparency: community and gender impacts

Symposium participations heard about the impacts of corruption at a community level. Corruption disproportionately affects the poor — and poor women in particular — because low levels of political and economic power limit their ability to hold states or the private sector to account.

In Indonesia, decentralisation programs and poor mining governance has resulted in foreign companies adopting risk aversion strategies, with many leaving the country. Decentralised systems of government have resulted in the granting of thousands of licences for mining, forestry and palm oil companies, with licences being issued two or three times over for the same piece of land. This has effectively resulted in the "democratisation of corruption". It was suggested that a "governance nightmare is the sweetest dream for the illegal economy". It was also noted that thousands of small-scale miners pay nothing in "official" revenue flows to government. Furthermore, illegal gold mining significantly harms people's health and the environment because of the use of mercury to extract gold. Initiatives such as EITI will only go so far in addressing challenges such as this.

As a result, communities are at risk of losing their very existence. The impact is greatest on women, who are "at the bottom of the pyramid" and often depend on the natural environment for their survival, and for providing food and medicines for their families. Mining can also indirectly increase the levels of violence against women and bring about change in women's traditional roles.

Key themes and trends

The symposium confirmed that the extractives sector is heavily exposed to risks of bribery and corruption. Business operations in high risk jurisdictions and a reliance on third parties and intermediaries contribute to those risks.

The relationship between poor governance and corruption became all too evident. This was discussed in the context of both the legal and illegal trade in natural resources, and culturally entrenched patronage systems. Resource nationalism emerged as a trend that will further test company policy and practice, and tax regimes. Nonetheless, the message was clear that extractive industry companies need greater regulatory attention and risk analysis. Similarly, financiers are increasingly aware that corruption costs can become financial risks for investors and mining companies themselves.

Acknowledgements

Oxfam Australia acknowledges the partnership with the Melbourne Business School and the support of Transparency International, which contributed to the symposium's success. We also acknowledge the willingness of all participants to actively discuss complex issues.

Resources

Oxfam Australia mining-related reports and other materials can be found at www.oxfam.org.au/explore/mining

Contact

Serena Lillywhite
Mining Advocacy Lead
Oxfam Australia
Telephone: +61 3 9289 9490
Email: serenal@oxfam.org.au

Christina Hill
Mining Advocacy Coordinator
Oxfam Australia
Telephone: +61 3 9289 9311
Email: christinah@oxfam.org.au

[2] The Australian Council of Superannuation Investors, "Anti-Corruption and Bribery Practices in Corporate Australia: A review of exposure to corruption and bribery risk across the S&P/ASX 200", CAER — Corporate Analysis. Enhanced Responsibility, October 2011

[3] Baker & McKenzie, "Bribery — Do Australian companies take it seriously?", Global Business Challenges, 2011/2012

OXFAM Australia