

EITI AND THE ROLE OF THE EMERGING ECONOMIES

A paper prepared for the EITI International Advisory Group (IAG) by the EITI Secretariat

1. Key Questions for IAG

- 1.1 Should the EITI Secretariat work to secure the support of companies and Governments of the emerging economies to the EITI principles and criteria (both in implementing countries and at a global level)?**
- 1.2 What role is there for different IAG members in this? Can companies lobby through local partners directly, or is this solely a government-to-government effort?**
- 1.3 What are the best levers for encouraging the engagement of the emerging economies?**

2. Introduction

2.1 Consumption of natural resources in the emerging economies (such as Brazil, Russia, India, China, South Africa etc) is rapidly increasing. China alone accounted for 40% of the growth in oil demand over the last 4 years. Associated with this, host companies from these economies are increasingly active in exploration and production in the extractive industries in resource-rich countries. Revenue and payments disclosure by such companies and countries would send a strong demonstration effect to potential EITI countries and ensure EITI is established as an international 'norm' for resource revenues management. Lack of transparency by such companies and countries has the potential to derail progress in improving resource revenue management made under EITI thus far, which in turn could lead to political instability, conflict and undermine security of supply.

2.2 The need for full involvement in EITI by non-OECD hosted oil, gas and mining companies has been raised by a number of EITI implementing countries as the most important determinant in the success of the initiative at the country-level. In addition, OECD-hosted companies concerned to ensure a level-playing field and at the impact corrupt business practices may have on the overall business climate in the countries in which they operate, have stressed the importance of a concerted effort to bring non-OECD companies into EITI. At their last meeting, IAG members asked the EITI Secretariat to prepare a paper on how to encourage emerging economy Governments to make public declarations of support to EITI, and to encourage their companies to participate in EITI in the countries in which they operate. This paper attempts to provide some analysis of the context and potential levers to prompt discussion.

3. Analysis

3.1 Increasing competition for oil, gas and mineral resources has led countries such as China and India to focus investment in politically-unstable resource-rich countries. For example the Government of India has invested more than \$1 billion in Sudan to acquire 25% stakes of the 5A/5B oil projects there; the Government of China has provided large, effectively condition-free oil-backed loans in Angola; Chinese companies have recently won bids in Sierra Leone, Gabon, Kazakhstan, Chad and Nigeria; Russian oil companies are very active in former-CIS countries. There is

concern that emerging economies companies' investment in these countries could introduce poorer business practices and lead to a deterioration in the overall business climate. For example, in Papua New Guinea, where the extractives sector has, until now, been dominated by US and Australian companies and is seen as broadly transparent, there is domestic concern that the planned new Chinese-operated nickel mine may lead to a reduction in e.g. health and safety standards, as well as less-transparency over payments and revenues.

3.2 In theory, countries that are implementing EITI should insist that all companies take part¹ and therefore emerging economy companies should be captured. Some countries have tried to achieve this through legislation (e.g. Nigeria passed a law annulling previous confidentiality clauses which prohibited countries from disclosing details, and mandating them to provide data on their payments). Some countries have tried a voluntary approach (e.g. Kazakhstan has encouraged companies to sign a MoU although not all have yet done so). Despite this EITI criteria requirement, the extent of cooperation from companies from the emerging economies differs considerably. For example, in providing full, accurate and timely returns which are clearly understandable, and in encouraging (or at least not discouraging) governments from taking forward implementation. In many countries, it is the local representatives from companies who will set the tone of the discussions and affect government decisions on whether or how far to implement EITI.

3.3 Few of the major emerging economies have shown interest in EITI so far. South Africa did attend the 2005 London conference as observers, but no progress has been achieved in subsequent dialogue with them. Russia also attended the 2005 London Conference as an observer and their companies are signatories to the Kazakhstan and Azerbaijan MoU, but there has been no unequivocal support from either the Russian Government or companies for EITI. Petrobras are a member of the IAG, but there was no Brazilian representation at the 2005 London Conference. Neither India nor China sent representatives to the Conference.

4. Levers

4.1 In the short-term, the key lever for encouraging EITI implementation is likely to be self-interest. Security of supply is a major concern to China, Russia and India in particular. At the moment the acquisition of energy resources is seen in terms of the fight to secure access to a finite resource. Instead there is a need to present the potential mutual benefit from encouraging long-term investment in production – thus facilitating supply stability – and the role of EITI as a part of this longer-term energy strategy. As more countries sign up to and begin implementing EITI, the evidence base for and understanding of how EITI can help to improve stability of supply should improve.

4.2 Over the medium-to-long term, a further incentive for greater company involvement from the emerging economies is their desire to become major multinational players, with the same status as IOCs such as Shell, BP, Chevron etc. This will involve them improving their own corporate governance and risk management procedures, and, to some extent, improving their international reputations by taking on the same kinds of

¹ Criteria no. 4 “this approach is extended to all companies including state-owned enterprises” (taken from the EITI Source Book, March 2005)

commitments and measures as OECD companies, such as support for the OECD Guidelines for Multinational Enterprises, and standards on transparency.

5. Possible actions

5.1 Support to EITI would not necessarily require the emerging economies to implement it themselves. Brazil, India, and China for example, are not target countries for EITI as they are not 'resource-rich', and other supporter countries, such as Australia (and UK) have not implemented EITI themselves. The focus should therefore be on attempting to persuade emerging economy Governments to make public declarations of support to EITI in resource-dependent countries, and to encourage their companies to participate in EITI in the countries in which they operate.

5.2 **Diplomatic (government-to-government) efforts.** Through the G8, EU and bilateral means to make the case for EITI with emerging economies' Governments. The UK have begun discussions with three major Chinese oil companies (a meeting with Petrochina and telephone discussions with Sinopec and CNOOC), as well as with representatives from the Shell office in Beijing. These have emphasised the need to engage the NDRC Energy Bureau, as the key centre for determining energy policy. There has also been strong US pursuit of this objective through both Washington and Beijing. The UK & US have also raised with the Russian authorities as part of G8 2006 discussions. *This could be further deepened with the inclusion of other donors.*

5.3 **Evidence-base.** The problems (poverty, conflict, corruption) that we know lack of transparency causes in resource-rich countries are well documented in academic literature. However, they are perhaps little understood by, or poorly-presented for, the emerging economies' audience. *The EITI Secretariat could produce a series of brochures aimed at non-OECD companies and consumer countries which draws together evidence on e.g. the impact of conflict on oil prices and supply volumes over the last 20 years.*

5.4 **Company/investor pressure.** Making improved corporate governance, risk management procedures or EITI compliance a condition of investor finance or for partnership with other international companies could be

5.5 **Direct (regulatory) pressure.** Reforms to international accounting standards and listings requirements would be the only way to guarantee all firms, including those in emerging economies companies (as and when they seek to raise money on the international markets) to support EITI implementation.

5.6 **Indirect (voluntary) corporate responsibility initiatives.** Through fora such as the UN Global Compact and OECD Guidelines for Multinational Enterprises encouraging firms to improve their international reputations by taking on the same kinds of commitments and measures as OECD companies.