

To the Ministry of Finance

24 March 2011

(UNOFFICIAL ENGLISH TRANSLATION)

Re: Recommendation to exclude companies that buy phosphate from Western Sahara

The Council on Ethics refers to the Ministry of Finance's letter of 7 February 2011, in which the Ministry requests further details on some of the aspects regarding the recommendation to exclude the companies Potash Corporation of Saskatchewan and FMC Corporation from the Government Pension Fund Global (GPFGL). The recommendation was submitted on 15 November 2010.

The recommendation examines companies which, through long-term contracts, purchase phosphate mined in Western Sahara by the Moroccan state-owned company OCP. Western Sahara is a Non-Self-Governing Territory without a recognized Adminstrating Power. In practice Morocco controls most of the area. In the view of the Council on Ethics, the companies' purchase of phosphate through contracts that specify the source as a mine situated in Western Sahara constitutes a serious violation of norms because the interests of the local population are not being considered and because OCP's operations contribute to maintaining the territory's unresolved situation.

The Ministry of Finance asks the Council on Ethics to elaborate on its understanding of the limitations of complicity as concerns purchases in general, as well as to comment on some issues related to the case at hand.

In its letter, the Ministry of Finance also refers to two previous recommendations. One of these is partly concerned with a company's responsibility for matters pertaining to its sub-contractors. In this case, the Council on Ethics attached importance to the influence that a company may exercise over a supplier by being its sole customer. The other recommendation emphasizes the extent to which a company contributes to sustain a state's violations.

In light of these earlier cases, the Ministry of Finance asks the Council on Ethics to clarify what actions would normally be considered contributive in a purchasing relationship, also as concerns the buyer's influence over any violation of norms on the part of the seller as well as the dependency-relationship between the two. The Ministry of Finance also requests the

Council on Ethics to comment on whether the seriousness of the activity in question may influence the standard of diligence against which companies are benchmarked, for instance in cases where the products purchased originate from occupied territories.

Firstly, the Council on Ethics notes the seeming inaccuracy in the Ministry's reference to this matter as a case in which the Council on Ethics recommends the exclusion of a buyer '*exclusively on the grounds of what the seller does*'. As previously mentioned, this is a case in which the buyer has specified where the phosphate is to come from, and not an instance of buying unspecified phosphate from a seller that also has other production sites within Morocco proper. Furthermore, the Council on Ethics has previously submitted a recommendation to exclude a buyer on the grounds of what the seller does: In 2006, the Council on Ethics recommended the exclusion of the company Monsanto Co¹ from the GPFPG due to an unacceptable risk of contributing to the worst forms of child labour in Indian hybrid cotton seed production. The Council on Ethics took as its point of departure that there was a clear connection between the company's operations and the use of child labour insofar as Monsanto's subsidiaries entered into agreements with local farmers about the cultivation of hybrid cotton seed while providing intermediate goods and controlling the production. Being fully aware that this type of cultivation commonly involved extensive use of child labour, Monsanto bought the seed without doing enough to prevent the practice. In that case, the Council on Ethics considered that the degree to which the company contributed to violations in its supply chain together with the seriousness of the violations indicated that the company should be excluded from the GPFPG.

The Monsanto case and the other cases referred to by the Ministry illustrate well how the link between companies in the GPFPG and norm violations will vary from case to case. The Council on Ethics does not assess a purchase situation or other forms of corporate relations separately from the underlying violation, but evaluates these against the nature and gravity of the violation and the concrete relationship between the buying and selling parties. It is therefore difficult for the Council on Ethics to offer an accurate description of all the factors which may constitute a contribution to violations in any given purchase situation, as this will indeed depend on the nature of the violation and the overall circumstances. In the case at hand, the Council on Ethics has assessed the companies' knowledge and specification of the product origin, the product's replaceability from the buyer's perspective, and the contractual relationship between the buyer and the seller. Similar factors may also be assessed in other cases where the Council on Ethics evaluates a company's contribution to the violation of norms in a given purchase situation.

In general, the Council on Ethics understands that the severity of the violation will determine how strict the company's obligation to avoid contributing to it will be. The section of the GPFPG's Ethical Guidelines that provides the foundation for the conduct-based exclusion of companies comprises, in principle, only serious violations. For the kind of cases that the Council on Ethics considers, it is therefore natural that strict diligence is required from companies to avoid contributing to the violation of norms.

¹ The Council on Ethics' recommendation to exclude the company Monsanto Co, 20 November 2006.

The assessment of companies that buy products which originate from occupied territories may give rise to a number of issues. To date the Council on Ethics has not submitted any recommendation that discusses this matter, nor has it based its evaluation of the present case on the grounds that Western Sahara is occupied. In terms of international law, there are very few areas in the world today that are under military occupation.

The rules of international law seek to delegitimize financial gains that stem from the exploitation of natural resources through occupation, precisely because access to natural resources may form the basis for violent conflict. Pillage is in any case illegal in occupied territories, and the occupying Power is obliged to refrain from pillage and also to prevent others from doing it.² With regard to mineral resource exploitation in occupied areas, it may be legal to continue mining activities that were in progress before the occupation occurred, whereas it may be illegal for the occupying Power to open new mines. On the other hand, it is possible that civilian needs, such as for coal or minerals for local industries, make it necessary to establish new mines. Such considerations must be weighed against each other. An assessment of a company's purchases of products from occupied territories must take into account the property rights to these products, for instance whether they stem from private property confiscated by the occupying Power or from public property in the occupied territory; whether the products are being sold by actors with similar operations in the area before it was occupied; whether the products are based on renewable or non-renewable resources, and so forth. In the case of Non-Self-Governing Territories such as Western Sahara, the requirement that the exploitation of natural resources must take place in accordance with the interests of the local population will be even stronger.³ It falls outside the scope of this letter to discuss the various and complex issues that may arise from such cases on a general basis. However, the main rule should be that companies must exercise great care if they are engaged in business activities in non-self-governing, occupied or disputed territories, or if they have commercial ties to companies with operations in such areas.

The Council on Ethics acknowledges that assessing a company's purchase of products of 'unethical origin' may pose difficulties in terms of delimitation, and it is also studying other areas where such issues are relevant. For example, if companies in the GPFG buy tropical timber that comes from states with an export ban, it may be appropriate for the Council on Ethics to assess whether the buyer is committing a serious norm violation. Another related topic is illegal or unregulated fishing. It may for example be relevant to analyse whether the

² A ban on the pillage of occupied areas is laid down by the Hague Regulations of 1907, art. 47, and the IV Geneva Convention, art. 33. In 2005 the International Court of Justice in The Hague (ICJ) pronounced judgement in the case *'Armed Activities on the Territory of the Congo (Democratic Republic of the Congo v. Uganda)'*, placing the exploitation of natural resources carried out by the occupying Power in the occupied territory in the same category as pillage (paragraph 245): *'Thus, whenever members of the UPDF were involved in the looting, plundering and exploitation of natural resources in the territory of the DRC, they acted in violation of the jus in bello, which prohibits the commission of such acts by a foreign army in the territory where it is present. The Court notes in this regard that both Article 47 of the Hague Regulations of 1907 and Article 33 of the Fourth Geneva Convention of 1949 prohibit pillage.'*

See <http://www.icj-cij.org/docket/files/116/10455.pdf>.

³ Article 73 of the UN Charter instructs administering Powers of Non-Self-Governing Territories to promote the well-being of the inhabitants and ensure economic advancement according to their interests.

purchase of fish by companies within the GPFG should be considered a serious violation if the fish was caught without a licence within a state's economic zone.

As the Ministry of Finance points out, the preparatory work to the GPFG's Ethical Guidelines states: *'Even if a company has unethical subcontractors, it may be sensible to refrain from excluding investment unless there is a pattern where the company uses the subcontractors with dubious practices without seeking to influence the situation. The situation will approach complicity if the customer relationship is long-term or repeated after the unethical practices have been identified.'*⁴ In this paragraph the preparatory work stresses that the buyer's awareness of the unethical practices, the lack of willingness to exit the customer relationship after the unethical practices have been identified, as well as the duration of this relationship may be relevant topics for evaluation.

Regarding the present case, the Ministry of Finance asks to what extent the companies that buy phosphate may be said to influence the underlying situation, or whether the situation would continue regardless of their continuing purchase of phosphate under long-term contracts.

In cases involving companies that contribute to violations of human rights or of international law, the formal responsibility will generally lie with the state. The role of the Council on Ethics is to assess the level of involvement in the violations on the part of companies, and the purpose of the GPFG's Ethical Guidelines is to avoid contributing to unethical practices. The Council on Ethics does not assess whether the exclusion of companies may have an impact beyond this, such as helping to improve the human rights situation or the political situation in a state.

In cases where the buyer's unethical behaviour is a result of the seller's lack of legitimate rights to the resources that are being sold, one issue for the Council on Ethics to assess may be whether the agreement between buyer and seller is comparable to commissioned theft when the buyer, being fully aware of the conditions related to the production, specifies the origin of the product.

In the present case one may also say that there are norm violations taking place at various levels: The companies commit violations by buying phosphate under long-term contracts from OCP, OCP commits violations by mining the phosphate without taking the interests of the local population into consideration, and the authorities commit violations by letting these business operations be conducted in such a way.

If the companies in question stopped buying phosphate through long-term contracts with OCP, the violation for which they may be blamed would obviously cease to exist. Beyond that, it is outside the scope of the Council on Ethics' competence to assess whether the situation in the area would change if the two companies included in the recommendation stopped buying phosphate from Western Sahara under long-term contracts.

⁴ NOU 2003:22, paragraph 5.3.2.3.

The Ministry of Finance also asks the Council on Ethics to comment on whether OCP's phosphate mining in Western Sahara would end if regular deliveries were discontinued. The Ministry's final request is a more detailed analysis of the extent to which companies that buy phosphate sporadically from Western Sahara must be considered to influence the underlying situation, compared with companies whose purchases are made under long-term contracts.

It is difficult for the Council on Ethics to form an opinion of which steps OCP would take under other circumstances than the current. At its meeting with representatives from OCP, the Council on Ethics was given somewhat conflicting information about the scale of its activities and the significance of long-term contracts. Still, the fact of the matter remains that if no companies in the GPFG portfolio buy phosphate under long-term contracts from OCP, the latter's operations and their effects would be immaterial for the GPFG and the Council on Ethics.

The deliberations underpinning this case build on an analogy with the obligations of administering Powers of Non-Self-Governing Territories. One of these obligations is to ensure that the exploitation of natural resources is carried out in accordance with the interests of the local population. In principle this will apply regardless of the contractual relationship under which the sale of natural resources occurs, being applicable to both long-term contracts and single purchases.

The Council on Ethics may only recommend the exclusion of a company if there is an unacceptable risk of future violations associated with the company's operations. This implies that sporadic buyers of phosphate from Western Sahara should not be recommended for exclusion, seeing as it will be difficult for the Council on Ethics to form a concrete opinion about the future risk of violations. According to the Council on Ethics' assessments, among sporadic buyers of phosphate from OCP there are no companies in the GPFG's portfolio that have purchased phosphate from Western Sahara in the past three years.

In addition to the different outcomes that an assessment of future risk would have for buyers with long-term contracts vis-à-vis sporadic buyers, the Council on Ethics finds that, as concerns the companies it recommends to exclude, the long-term contracts link them more closely to OCP's violations. Not only are these companies aware of the origin of the phosphate, they have placed orders specifying that it should be mined in Western Sahara.

Yours sincerely,



Gro Nystuen
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