



The Council's work under the corruption criterion

In Section 3 of the GPFG's ethical guidelines, it says: "Companies may be put under observation or be excluded if there is an unacceptable risk that the company contributes to or is responsible for gross corruption."



A two-stage process underpins the Council's recommendations to place a company under observation or exclude it under the corruption criteria. First, it must be possible to determine that there is an unacceptable risk that a company has been involved in gross corruption. Thereafter, the Council assesses whether there is an unacceptable risk that the company may become involved in new corruption allegations. Both these conditions must be met before the Council will recommend observation or exclusion under the corruption criterion.

The most important sources of information for the Council's investigations relating to corruption cases are news reports and the work of investigative journalists, disclosures by public prosecutors or final verdicts, judgements or out-of court settlements. Occasionally, reports by civil society organisations may also contain information that is sufficiently specific to be used in the Council's assessments. Access to this type of information varies considerably in the different countries in which GPFG companies are registered or have their international operations. A fundamental challenge is that corruption risk is normally higher in those countries in which access to information from the media, judicial system, civil society organisations and the companies themselves is more restricted and unreliable, such as countries with authoritarian regimes.

Companies that are selected for further examination on the basis of the preliminary review of the corruption allegations made against them are systematically registered, sorted by sector and ranked with respect to their level of risk. This list is constantly being updated and expanded. Within certain sectors, allegations have been noted against such a large number of companies that it is possible to perform a more collective analysis of them.

In 2020, the Council issued one recommendation to exclude under this criterion. The Council recommended the exclusion of the Chinese oil company PetroChina Co Ltd, because it demonstrated little willingness to cooperate with the Council. At that

point, the company had been under observation since May 2017. In the Council's opinion, the company's lack of assistance in clarifying the case prompted questions about PetroChina's true willingness to prevent, detect and deal with corruption. In general, the Council considers it vital that companies under observation are willing to share information if the arrangement is to work as intended. In August, Norges Bank decided to follow up the company through active ownership.

The Italian defence company Leonardo SpA has been under observation since 2017. Due to the pandemic, it was not possible for the Council to meet with the company as planned in 2020. The 2020 observation report has therefore been postponed until 2021.

With respect to the corruption criterion, the Council devoted most time in 2020 to ongoing investigations into several companies, five of which have been given particular priority. Of these five, three belong to the Industrial Goods & Services sector⁵, while the remaining two are companies that were selected on the basis of the Council's 2019 review of oil service companies. In 2020, The Council has issued a recommendation to place one of these companies under observation.

In addition to its work relating to individual GPFG companies, the Council also strives to participate in and contribute to forums and processes in which anti-corruption is a key element. In 2020, the Council attended the World Bank's Fifth International Debarment Colloquium and Transparency International's 19th International Anti-Corruption Conference (IACC). As far as the Council is aware, its model – under which decisions to exclude or place companies under observation are made public – remains rather unique among the major sovereign wealth funds. The Council finds that there is a fair degree of international interest in this model, as a new and alternative measure in the anti-corruption field.

5 See FTSE Russell, February 2019: *Industry Classification Benchmark (Equity)*, https://research.ftserussell.com/products/downloads/ICB_Rules.pdf



Corruption linked to state-controlled oil companies

Since the Council started systematically monitoring the GPFG's portfolio with respect to corruption, the oil and gas sector has produced the second highest number of recorded cases. The sector with the most recorded cases – Industrial Goods & Services – is a very heterogeneous “supersector”, which also includes companies that supply the oil and gas industry. This picture accords with the findings of international surveys, where oil and gas stands out among the sectors with the world's highest corruption risk.

The high level of corruption risk must be seen in light of several factors. The exploitation of natural resources is traditionally associated with extraordinary returns (economic rent), which in and of itself may provide strong incentives for corrupt behaviour. Furthermore, oil and gas production projects are often extremely complex, consisting of many different components and actors, which can make it very challenging for an outsider to gain an overview of what is going on. The projects are also often large and long-lasting. It can take several years before the companies concerned receive a return on their invested capital. This can make it more difficult to resist any demands for bribes that may be made during the course of the project.

However, the main challenge relating to corruption risk in the oil and gas industry is, perhaps, that much of the world's oil and gas resources are located in countries with weak governance, an absence of democracy and weak institutions. In several of these countries, a wealth of natural resources has proved not to make a positive contribution, but has instead reinforced these negative societal features. This phenomenon is often referred to as the “resource curse”. The authorities in these countries have increasingly secured for themselves direct control over the extraction of oil and gas resources through the establishment of state-controlled oil companies, also known as National Oil Companies (NOCs), in which the state owns more than 50 per

cent of the shares. Where NOCs lack financial resources, technology or competence, they often form joint ventures with major international oil companies (IOCs). According to the Natural Resource Governance Institute's NOC database, there are a total of 71 NOCs in 61 countries worldwide. NOCs account for around 55 per cent of the world's oil production and control approx. 90 per cent of global oil and gas reserves.⁶ Almost all of the NOCs are in countries outside the OECD, the vast majority of them in countries with a high or extremely high corruption risk, according to indexes produced by Transparency International or the World Bank.

The corruption risk associated with NOCs is primarily a matter of *passive* corruption. In other words, the people in authority, who control the award of licences, procurement contracts, etc, demand or accept bribes from companies in return for choosing them as the operator, supplier, building contractor, and the like. In addition, corruption may include different forms of embezzlement and financial misconduct, where a portion of the NOC's revenues are syphoned off before they end up in the nation's coffers. These bribes or misappropriations may be channelled into private pockets, but may also be misused by governing political parties in connection with election campaigns and to buy support.

Some of the NOCs in the GPFG's portfolio have already been investigated for corruption (Petrobras and PetroChina, for example). However, the Council has not previously carried out a collective review of such GPFG companies. A review of this kind got underway in the autumn of 2020 and will continue in 2021.

⁶ National Resource Governance Institute. 2019. *The National Oil Company Database*, https://resourcegovernance.org/sites/default/files/documents/national_oil_company_database.pdf.