

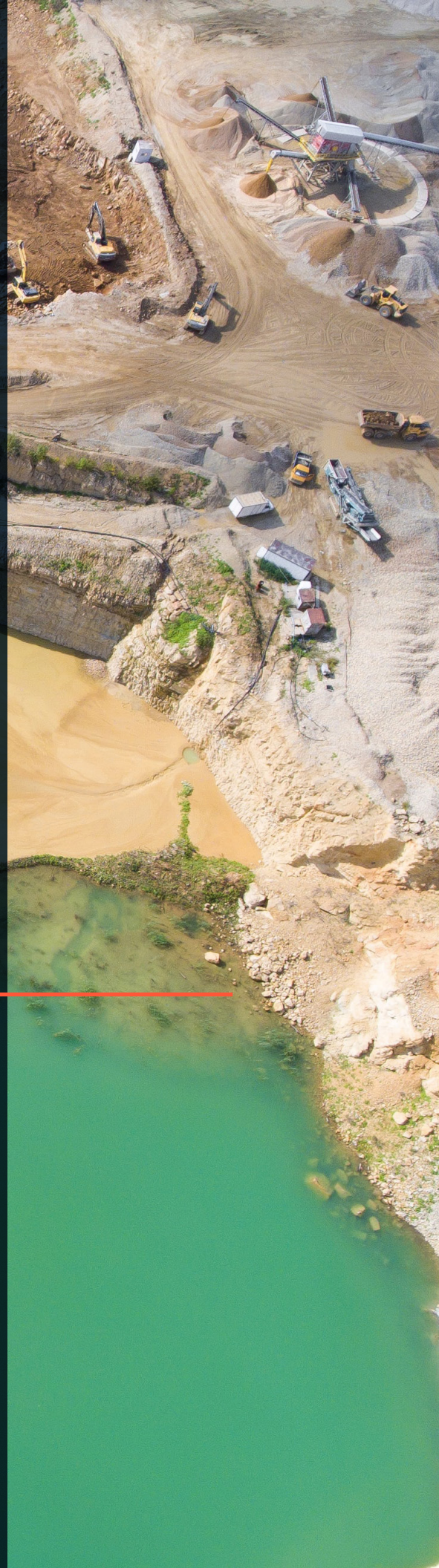


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Anticorruption Guidance for Partners of State-Owned Enterprises

Full Guidance

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Full Guidance

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Anticorruption Guidance for Partners of State-Owned Enterprises

Drawing on broad stakeholder consultations, corruption case analysis and reviews of existing best practices, this guidance proposes concrete measures that companies should adopt to reduce corruption risks in their work with state-owned enterprises (SOEs) in the oil, gas and mining industries. It also recommends measures SOEs can take to strengthen their anticorruption safeguards.

The guidance for private-sector companies has five parts:

1. Conducting due diligence on SOEs
2. Avoiding high-risk agents
3. Responding to political exposure
4. Safeguarding payments
5. Protecting joint ventures from corruption

The final section identifies corresponding recommendations for SOEs in each of these five areas.

By adopting stronger safeguards against corruption, international companies and SOEs can avoid costly scandals that hamper their performance and damage their reputations. These reforms would also help protect the interests of resource-producing countries. Past cases clearly show the kinds of economic, social and political damage corruption can cause.

The guidance and accompanying materials are available online at resourcegovernance.org/soe-anticorruption.

The challenge

A significant share of recent corruption cases in the oil, gas and mining industries have implicated state-owned enterprises (SOEs). Private-sector companies played a role in nearly all these cases too, either directly or indirectly. As this record makes clear, standard corporate integrity and compliance systems are often poorly suited to address the unique position and powers of SOEs. In many host countries, SOEs play dominant and pervasive roles and maintain close relations with the political leadership. Often the only way for private companies to work in a country is to partner with the SOE, and smooth operations often depend on securing and maintaining the SOE's favor. Companies can choose to avoid certain third parties when concerns arise, but working with SOEs—even those that exhibit major red flags of corruption—rarely seems optional. Similarly, companies cannot simply push their integrity standards and compliance systems onto an SOE given its level of influence.

While SOEs and their partners often operate with integrity, corruption is common and harmful enough to deserve special attention. Many recent cases have revealed SOE officials receiving bribes, steering overly lucrative deals to politically connected parties, or misappropriating SOE funds. In other instances, private companies instigated the corruption, lured by the lucrative opportunities SOEs can offer. In some countries, these and other forms of SOE corruption are chronic and reinforced by the prevailing political context. SOE corruption often inflicts harms on society, including lost public revenues, weak sector performance, damage to host communities, lost investment and slowed economic growth, entrenched authoritarian regimes, public frustration and distrust, and even political unrest and conflict.

Many companies and SOEs are working to prevent corruption, creating opportunities for progress. Past corruption scandals created serious legal, reputational or commercial consequences for many SOEs and their corporate partners. Environmental, social and governance (ESG) factors including around integrity have gained influence within the sector, and risks accepted years ago are no longer tolerable for many industry players. Some companies and SOEs have adopted valuable anticorruption reforms which, if adopted more widely, would help clean up and level the industry's playing field. Meanwhile, past cases offer valuable lessons about the sector's greatest corruption vulnerabilities and how they might be fixed. The guidance presented here builds on these openings.

Approach

The guidance derives from three main sources. First, over a two-year period beginning in December 2019, NRGi convened and consulted more than 110 individuals from over 50 organizations, including compliance personnel and other representatives from 18 large oil, gas and mining companies, several SOEs and many anticorruption experts and activists. Along with one-on-one interviews with participants, NRGi held workshops on each of the guidance's five topics in November and December 2020.

Second, NRGi studied over 100 extractive sector corruption cases to identify common trends and possible remedies.

Third, NRGi reviewed and drew from other anticorruption and compliance guidance published by law enforcement agencies, international bodies such as the UN, the World Bank and the OECD, companies and non-governmental organizations, as well as materials and standards related to SOE and resource governance. (For a list of key sources, see the references section of the full guidance.)

The guidance has several defining attributes that distinguish it from existing tools and frameworks:

Sector- and SOE-specific. Extensive guidance is available for companies on establishing internal compliance systems and managing third-party risk, but it does not focus on SOEs or the extractive sector—both of which present specific challenges.

A mix of basic and ambitious measures. Some recommendations contained in the guidance represent good practices that many companies have already adopted and that should be mainstreamed across the industry. Others are more forward-looking and ambitious and will carry commercial costs, but target demonstrated areas of risk. As a result, certain recommended measures are more difficult to implement than others. Taken as a whole, however, the guidance here reflects the practices that companies should adopt if preventing corruption and the consequent harms are a top priority.

Problem-focused. The guidance is not comprehensive. Its five topics emerged from the consultation process as challenging areas where more learning and improved practices are needed. Other important anticorruption topics, such as bribery, facilitation payments, gifts and hospitality, are not a focus, though many other anticorruption resources address these.

Prioritizing the public interest in producing countries. NRGi is a non-profit organization that works to promote effective, accountable and sustainable resource governance, especially in developing countries. This brings a different orientation from that of many sources of compliance guidance, which traditionally prioritize a company's desire to avoid legal liabilities. This focus explains several of the guidance's cross-cutting themes:

- ▶ **How companies can avoid enabling corruption.** Companies should actively work to avoid enabling the diverse forms of corruption that occur frequently in the extractive sector, including its more systemic forms.

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- ▶ **Assessing and avoiding potential societal harms.** Because SOEs manage public resources, SOE corruption can inflict serious harms on the public interest. While there are limits to their influence, companies should incorporate awareness and assessments of societal harms into their anticorruption approaches, and use this as a factor to determine risk and inform decision-making (alongside e.g., the company's own reputational and legal concerns).
- ▶ **Reducing subjective case-by-case decisions.** Past corruption cases indicate that a full reliance on case-by case discretionary decision-making can, in certain instances, fail to protect the public interest. Under pressure to advance a deal, company personnel have elected to accept serious corruption risks. In some cases, scandal, legal action and societal harm followed suit. In response to this trend, the guidance recommends that companies adopt several upfront rules, such as limitations on working with certain high-risk third parties, that would help reduce the number of *ad hoc* decisions company personnel must make.
- ▶ **Transparency, including the disclosure of rules and policies.** Many of the recommendations urge companies to disclose information about their engagements with SOEs. In particular, companies should tell the public more about their approach to managing corruption risks, including the rules they have in place around agents, politically exposed persons, conflicts of interest, payment controls and other priority topics. By disclosing these rules, a company signals its commitment to integrity to current and prospective third parties, staff, investors and other key stakeholders including citizens. Public disclosure of company rules discourages exemptions and avoidance, and may motivate other industry players to follow suit.

The guidance

The first five sections of guidance presented below are primarily intended for three categories of company that engage extensively with SOEs—those involved in exploration and production, the supply of goods and services, and commodity trading—but many of the recommendations also apply to SOE lenders, investors and financial service providers. Within these firms, compliance and legal departments would lead on implementing many of the recommendations. The final section of the guidance contains recommendations for SOEs.

Civil society groups, parliamentarians, anticorruption commissions and other oversight actors could also use the guidance when pressing for reform and evaluating whether investors and SOEs are adequately preventing corruption. Finally, the guidance could inform other governance and anticorruption standards, in the extractive sector and beyond.

Note: For the purposes of this guidance, private-sector companies that partner with SOEs are referred to as “companies” and state-owned enterprises, while also companies, are referred to as “SOEs.”

1. Conducting due diligence on SOEs

The challenge

While standards vary significantly, a broad and diverse set of state-owned enterprises (SOEs) have proven vulnerable to corruption. NRGi has identified over 100 relevant cases of corruption involving oil, gas or mining SOEs. Because SOEs are entrusted with managing their country's natural resources, accountability shortfalls can cause serious damage: sector underperformance, deterred investors, fewer revenues for public services, entrenched kleptocracy, and even disenfranchisement among citizens and political instability.

As these past cases help illustrate, SOEs have a unique and complex risk profile which standard corporate due diligence approaches were not designed to address. To prevent legal, commercial and reputational costs and avoid enabling corruption that harms the countries where they work, companies should invest in enhanced due diligence approaches.

Carrying out effective SOE due diligence and acting on the findings are not straightforward tasks. Companies have highlighted several difficulties:

- ▶ Compared to other third parties, companies view SOEs as relatively unavoidable partners because:
 - ▶ they are often required to partner with an SOE to invest in a country.
 - ▶ exiting an SOE relationship carries high costs, especially for producing companies which have invested substantial capital in long-term projects with SOE partners.
 - ▶ SOEs are powerful, which causes companies to hesitate before raising concerns or pushing remediation measures too hard.

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- ▶ avoiding SOEs with corruption problems would close off too many opportunities. Some companies tend to accept SOE corruption as part of doing business, and simply aim to avoid direct involvement.

As a result, companies may invest less in SOE due diligence because its findings are less actionable. For the reasons noted above, companies would often still work with an SOE even if the due diligence found many serious red flags.

- ▶ SOEs exist as integral and influential components of a country's political and economic system. They cannot be assessed independently of the wider country context.
- ▶ Adding to the complexity, SOEs typically play multiple roles, from acting as producers and marketers to functioning as regulators or quasi-treasuries.
- ▶ Good information on an SOE's compliance performance can be hard to obtain. Public data is missing in many cases, and what does exist may not cover the informal roles and systems that influence SOEs. Asking for information on compliance effectiveness or past governance problems can also lead to tensions, which makes some companies tiptoe around the subject.
- ▶ It can be hard to know where to stop. SOE operations can be vast in scale, with many subsidiaries and hundreds of partners and associated organizations, all with potential challenges. It is also unclear how far back reviews should go.
- ▶ Since SOE executives qualify as politically exposed persons (PEPs), the corruption risks associated with PEPs (such as conflicts of interest or cronyism) are more likely to be present in SOE interactions. It is difficult to identify when political or personal motives may be driving SOE behavior.
- ▶ The evidence collected during due diligence often includes assumptions, unsubstantiated rumors and incomplete information, especially when describing informal political relationships. Hearsay is more difficult to document and record.

Companies are responding differently to these challenges. Many classify SOEs as high-risk counterparties and conduct extensive due diligence, particularly ahead of long-term relationships such as joint ventures. Following this process, some companies have decided against partnering with high-risk SOEs, or have put in place extensive risk-mitigation measures.

Yet practices appear uneven. In several scenarios, companies reported that SOEs receive only basic due diligence, such as standard know-your-customer, denied-party or adverse media checks. This limited approach occurs most often when:

- ▶ SOEs are long-standing partners, located in low-risk countries or seen as unavoidable (i.e., the company has already decided to accept the big-picture risks).
- ▶ The deals in question are short term and high volume, e.g., traders buying cargoes of oil.

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- ▶ The SOE is a client and companies fear harming their chances of winning business, such as when suppliers seek a contract from an SOE.

Even in such scenarios, effective SOE due diligence can protect companies' interests, as well as those of the public. The Petrobras "Car Wash" scandal centered in Brazil shows that even SOEs with strong commercial performance and corporate governance structures can be afflicted by corruption. Over USD 2 billion was lost to corruption between 2004 and 2012 through "massive bid-rigging and bribery schemes" in which illicit funds were shared between Petrobras, its contractors, intermediaries and Brazilian political parties.¹ Companies could have picked up the warning signs before the investigation went public in 2014. Petrobras had been connected to the *Mensalão* scandal, a corrupt vote-buying scheme which broke in 2005.² The company's executive management team was packed with political loyalists and its procurement systems exhibited red flags such as a heavy overreliance on "invitations to bid" and single-source contracting.³

Had various counterparties spotted these risks and responded seriously they may have avoided certain downsides. Several Petrobras suppliers have faced investigations and fines,⁴ and investors have taken Petrobras to court to recover USD 2.95 billion in losses stemming from the impact of the scandal on the company's share price.⁵ The following recommendations can help companies more fully identify and respond to corruption risks.

Recommendations

These recommendations draw on existing good practices and push for the kind of SOE due diligence that will help prevent corruption and the harms it causes. They apply to:

- ▶ oil or mining companies partnering with an SOE on exploration or production activities, including through operated or non-operated joint ventures
- ▶ trading companies that buy or sell commodities from or to SOEs
- ▶ service companies seeking supplier contracts from SOEs or joint ventures that include SOEs
- ▶ financial institutions that fund SOEs or projects to which the SOE is a party.

1 U.S. Department of Justice, "*Petróleo Brasileiro S.A. – Petrobras: Deferred Non-Prosecution Agreement and Statement.*" (2018)

2 Financial Times, "*Brazilian prosecutors arrest former Lula aide in Petrobras probe.*" *Financial Times*, 3 August 2015.

3 Petrobras operated outside the national procurement framework and generally followed simplified procurement processes. Between 2011 and 2014, 45 percent of contracts were awarded without competitive bidding. The remainder were awarded through "invitation to bid" agreements, whereby managers had discretion to choose which companies to invite to a tender. For more information, see Natalia Rezende de Almeida Santos, *Internal controls and corruption: the case of Petrobras*. Sussex Centre for the Study of Corruption (2017).

4 Jonathan Watts, "*Operation Car Wash: Is this the biggest corruption scandal in history?*" *The Guardian*, 1 June 2017.

5 Brendan Pierson, "*Petrobras to pay \$2.95 billion to settle U.S. corruption lawsuit.*" *Reuters*, 3 January 2018.

1. Companies should supplement their standard due diligence approaches to address the distinct risk profile of SOEs.

To strengthen standard due diligence procedures, companies should implement the following measures:

1.1. Conduct SOE due diligence in a manner that influences business decisions.

Due diligence is only useful if it is given adequate time and resources, and influences business decisions. In some cases, SOE due diligence is still seen as a box-ticking exercise, carried out to comply with policies rather than inform decisions. Some companies have proceeded with relationships when simple due diligence would have revealed overwhelming concerns, or have disregarded the findings that revealed these problems.

To avoid enabling corruption and reduce reputational and commercial risks, the due diligence process should:

- ▶ take place before a deal has acquired too much momentum
- ▶ involve legal and compliance personnel and high-level commercial decision-makers
- ▶ incentivize decision-makers to avoid taking risks
- ▶ explicitly aim to avoid enabling corruption and causing societal harm
- ▶ take place regularly for longer-term engagements. For existing partnerships, monitoring and responding to risks as they evolve is crucial. As the OECD observes, “The due diligence process is not static, but ongoing, responsive and changing. It includes feedback loops so that the enterprise can learn from what worked and what did not work.”⁶

At a minimum, due diligence findings should influence the risk management strategies a company employs. For instance, if there are red flags around procurement processes, the company should only participate in tenders which are transparent and competitive. If the SOE’s commercial and regulatory roles are in conflict, companies could set up barriers between their own teams that engage with the SOE on these matters. If agents played a role in past corruption schemes, the company should not use agents with this SOE (see Section 2). If risks of misappropriation run high, companies should prioritize the payment controls proposed in Section 5. There are many possible variations, but fundamentally an effective due diligence strategy must respond to the risks observed.

Yet mitigation cannot match every corruption challenge. Walking away should remain an option. Companies active in the oil, gas and mining sectors are often described as having high

6 OECD, *OECD Due Diligence Guidance for Responsible Business Conduct (2018)*, p.17.

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appetites for risk, as evidenced by their close collaboration with SOEs with troubling legacies of corruption. However, there are scenarios where deferral to this risk appetite is inappropriate, and where there is an ethical case not to proceed. To reduce inconsistency in decision-making and signal their commitment to integrity, companies could adopt minimum standards, such as prohibitions against forming a partnership when:

- ▶ there is clear evidence that the revenues generated will be misappropriated
- ▶ the partner engages in regular, harmful corruption with no evidence of intent to reform
- ▶ the partnership will benefit and entrench corrupt individuals or networks
- ▶ the partner lacks even basic integrity controls, e.g., a minimum level of financial transparency.

1.2. Examine the political and economic context in which the SOE operates.

To understand an SOE more fully as a possible partner, companies should invest in analyzing how the SOE fits into the country's wider political and economic context. Answering questions such as those proposed below can provide important background information for other parts of the due diligence, including the assessment of corruption risks. The findings can also help company personnel to look at SOEs more holistically, rather than focusing too narrowly on a specific transaction, and in doing so to better predict how the SOE might behave in the future. A range of publicly available sources contain helpful information.⁷

Political position. SOEs tend to have multifaceted relations with the state, commonly exercising great power and autonomy while also being susceptible to political interference. The political context will consequently impact the corruption patterns and pressures relevant to the SOE.

Due diligence reviews should ask questions such as:

- ▶ What role does the SOE play in the political system (e.g., supporting political patronage, providing a source of ready cash, helping fulfill campaign promises)? For example, in certain authoritarian regimes held together through systemic corruption, an SOE can be an integral part of how a dictator remains in power, and little daylight exists between the SOE and the regime. In countries with competitive political systems, incumbent politicians have used SOEs as sources of funding and patronage to help their chances of winning elections.
- ▶ Which government entities are charged with shaping and evaluating the SOE's performance, formally and informally? What power dynamics prevail in the relationships between the SOE and these supervisory entities?

⁷ Useful sources for this type of assessment include disclosures made by the SOE, including in its annual and financial reporting; Official government documents (audits, governance reviews, briefings); EITI reports; civil society reports; World Bank and IMF reports; NRCI's National Oil Company Database; Freedom House's Freedom in the World Index; Civicus's Civic Space Monitor; Bertelsmann Stiftung's Bertelsmann Transformation Index; V-Dem's Varieties of Democracy Index; Worldwide Governance Indicators on Voice and Accountability and Control of Corruption.

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- ▶ How involved are political figures in SOE decision-making? Do political figures regularly influence SOE decisions, formally or informally, such as the selection of partners, investments, procurement and hiring? Or does the SOE operate autonomously, or even at odds with the political leadership? How have changes in government impacted the SOE, and what does this say about its political ties?
- ▶ What are the key political events on the horizon (such as elections, transitions in political leadership, conflict) or ongoing governance or anticorruption reforms, and how could these affect the SOE? Examining trends can help companies understand the forces that favor SOE reform and how they might use their influence to support improved governance (see Recommendation I.6).
- ▶ How open and free is the space for civil society? Can journalists and activists examine and criticize the SOE without fear of recrimination?

Economic position. SOE financial data helps tell the story of an SOE's role within the country's economy. For instance, if the SOE retains an unusually large portion of its gross revenues and fails to turn a profit or pay dividends (especially during high-price periods), it may exist to pursue motives other than maximizing returns to the national budget. In these situations, political motives may dominate decision-making. Examples include when SOEs spend heavily on public goods (e.g., *Petróleos de Venezuela, S.A.* under Hugo Chavez), serve energy security purposes (e.g., Chinese national oil companies during recent decades) or allocate political patronage (e.g., *Sonangol* under José Eduardo dos Santos in Angola).

Data points that provide useful context include:

- ▶ volume of production and reserves, and their estimated value
- ▶ main sources of revenues, including commodity sales
- ▶ gross revenues (total, as a share of GDP and as a share of government revenues)
- ▶ transfers to government (total, as a share of gross SOE revenues and as a share of total government revenues)
- ▶ transfers from government
- ▶ net income (profits) and dividend payments to shareholders (if any)
- ▶ capital and operational expenditures
- ▶ liabilities and debts (total and as a share of total public debt)
- ▶ number of employees.

To interpret SOE financial data, it is useful to examine trends over time and to compare the data with that from similar SOEs.⁸

⁸ NRG's National Oil Company Database contains financial data from 71 national oil companies. www.nationaloilcompanydata.org.

1.3. Identify the leading corruption risks, their potential harms and whether the engagement might directly or indirectly contribute to them.

As part of their due diligence, companies should assess the forms of corruption an SOE has been involved in or could be in the future, the potential harms this corruption could lead to, and whether their activities might enable or entrench this corruption. A company should examine the entire SOE and all its functions, not just the specific unit or transaction at hand. As noted in 1.1 above, these findings would help inform important company decisions. If the risk of enabling harmful corruption runs very high, the company should avoid the engagement. Otherwise, the findings can help the company design appropriate mitigation and monitoring systems.

Step 1. Examine whether the SOE exhibits common corruption risks.

Past SOE corruption cases exhibit some common patterns. NRCI's review of over 100 cases found that seven main forms of corruption appear across a diverse set of SOEs. In their due diligence, companies should explicitly look to identify corruption risks in all these seven areas:

- ▶ Companies pay bribes or engage in collusion to win licenses or contracts from the SOE. Bribery is often carried out in collaboration with agents (see also Section 2).
- ▶ Officials unduly favor certain parties in SOE licensing and procurement.
- ▶ Officials hold commercial interests in the sector which create conflicts of interest or otherwise improperly influence their decision-making.
- ▶ Companies pay bribes to influence SOE regulations and approvals.
- ▶ Officials unduly favor certain parties in the SOE's regulatory activities and approvals.
- ▶ Officials misappropriate or embezzle SOE funds (see Section 5 for detail).
- ▶ Companies or officials unduly influence the laws and rules that govern the SOE and its activities, such as ensuring the rules enable discretionary decision-making, steering financial flows into preferred accounts or reducing corporate tax or regulatory burdens.

Companies should identify and focus on the forms of corruption that appear most likely, using evidence including past corruption cases, the presence of red flags and warning signs (see box below), existing governance weaknesses (see 1.5 below), feedback from experts and stakeholders, and other sources.⁹

⁹ In this review, companies will need to draw on multiple information sources, including media reporting, NGO investigations and reports, corporate records, offshore leak databases, beneficial ownership disclosures, court documents, regulatory investigations and research reports. Companies could also interview current and former SOE officials, personnel from different types of company, sector and country analysts, journalists and civil society activists.

The box below lists some of the warning signs that may accompany these forms of corruption. Scanning for these and other red flags could help companies to identify the leading corruption risks.

Red flags for corruption related to SOEs

Note: The presence of red flags does not necessarily indicate corruption has taken place, but rather that further scrutiny is warranted.

SOE-run licensing, contracting and procurement

- ▶ Licensing or procurement processes limit healthy, advisable competition—e.g., the single-source award of large contracts that interest many companies.
- ▶ Licensing or procurement processes deviate from established laws and regulations.
- ▶ Contract terms deviate from commercial norms, e.g., inflated contracts with suppliers or overly favorable prices for commodity traders.
- ▶ SOEs award contracts for unrealistic or unnecessary services.
- ▶ SOEs award contracts to companies that:
 - ▶ are unqualified or have a history of controversy or criminality
 - ▶ appear to be obscuring the identity of their true owners, e.g., through chains of shell companies in offshore jurisdictions
 - ▶ have politically exposed persons among their key personnel or beneficial owners.
- ▶ Certain firms win lots of awards in ways that do not seem commercially justifiable.
- ▶ Political loyalists with limited relevant experience are placed in jobs that control valuable license or contract awards.
- ▶ Licensing or procurement processes involve agents or intermediaries.
- ▶ An official intervenes in an award process, resulting in benefit to a particular company.
- ▶ An official involved in the award has a conflict of interest.

Regulatory activities

- ▶ Officials give biased or preferential treatment to certain companies in administrative process or when enforcing the rules.

- ▶ Known violations go uncorrected or unpunished.
- ▶ Certain companies are rumored to have a patron, ally or hidden owner who exercises influence over the enforcement of rules.
- ▶ Political loyalists with limited relevant expertise are placed in “gatekeeper” jobs that control important approvals.

Misappropriation

- ▶ SOE expenditures deviate from the prevailing rules, such as *ad hoc* withholdings from the treasury or quasi-fiscal, extra-budgetary expenditures on non-extractive activities.
- ▶ Audits, International Monetary Fund reports or other reviews raise concerns about the SOE's financial practices.
- ▶ The SOE's performance or transactions diverge from market realities—e.g., the SOE is not profitable during high-price periods, or sells assets or commodities at very low prices.
- ▶ The SOE spends large quantities of money on goods and services outside the oil, gas or mining sector that would typically be financed through the national budget.

Rulemaking

- ▶ Changes to the laws and regulations that govern the SOE unduly benefit a certain group, harm the interests of the state, or result in notable weaknesses.
- ▶ Rulemaking deviates from standard processes (e.g., long delays, fast-tracked decisions, or lack of consultation or transparency).
- ▶ Political loyalists with limited relevant expertise dominate rulemaking processes.

Weak enforcement of rules and integrity measures

- ▶ There is an implementation gap between the formal rules that govern the SOE's activities, and actual practices. Rules are not followed.
- ▶ When credible corruption accusations arose in the past, e.g., bribery cases instigated by foreign authorities, the SOE did not investigate or sanction the individuals involved.
- ▶ Companies implicated in corruption continue to work with the SOE.

Further governance, oversight and transparency gaps

- ▶ See Recommendation 1.5 below.

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Step 2. Assess whether the risks identified could lead to societal harms.

For the identified corruption concerns, companies should consider the harm these practices might have on society, in addition to assessing the commercial, legal, regulatory or reputational risks they may create for the company. In some situations, the forms of corruption identified may be legal under the laws of the host country. This does not reduce their capacity to cause societal harm.

The answers will rarely be clear cut, but it can help to bring together representatives of different divisions to consider a consistent set of questions, such as:

- ▶ What harms have resulted or could result from this form of corruption? They might include:
 - ▶ lost public revenues
 - ▶ reduced competition, efficiency and performance in the sector
 - ▶ reduced investor confidence
 - ▶ entrenchment of corrupt monopolies and unfair insider access to public resources
 - ▶ environmental damage and other harms to host communities
 - ▶ economic stagnation
 - ▶ undermining of democratic processes
 - ▶ conflict and political unrest
 - ▶ loss of public faith in state institutions¹⁰
- ▶ Is this form of corruption isolated and infrequent, or systemic?
- ▶ Are past problems resolved or outstanding? Is the SOE taking or likely to take remediation measures? In response to credible past allegations, has the SOE or government investigated and imposed penalties where appropriate?

Step 3. Assess whether the transaction or partnership is likely to contribute to the leading corruption risks.

- ▶ Would the transaction directly contribute to or worsen the issues? For instance:
 - ▶ Is the transaction likely to unduly benefit a politically connected company?
 - ▶ Is the SOE likely to misappropriate the specific payments involved?

¹⁰ On the costs of corruption, see, for instance: IMF, *Corruption: Costs and Mitigating Strategies*, IMF Staff Discussion Note (2016); A. Gillies, *Crude Intentions: How Oil Corruption Contaminates the World* (Oxford University Press, 2020); UNODC, *Effects of Corruption* (accessed 2021).

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- ▶ Would the transaction indirectly contribute to or worsen the issues, i.e., could the company end up enabling corruption? For instance:
 - ▶ Will the transaction legitimize the SOE despite its substantial and harmful corruption problems?
 - ▶ Will the transaction enable the SOE to raise funds to help a kleptocratic regime survive? Will it help political elites unduly acquire wealth or otherwise benefit from the sector?
 - ▶ Is the partnership likely to help a corruption scheme to function, e.g., by providing access to financing, international markets or technical capacity?
 - ▶ Will the transaction create or worsen a conflict of interest?

1.4. Identify the SOE's roles and the potential conflicts among them.

Companies may need to structure their engagement in ways that protect against conflicts among the SOE's roles. Such a scenario could arise if, for instance, the SOE regulates commercial entities in which it holds shares, or retains large revenues for its own expenditures rather than maximizing financial returns to the state. While not included in many traditional considerations of corruption, these conflicts can result in corruption-like behavior. Common definitions of corruption involve the abuse of entrusted power for private gain. In these scenarios, the SOE might act to advance its own interest at the expense of carrying out its public mandate.

Some SOEs have developed effective systems for managing conflicts of interest, such as by creating clear barriers between these functions. In other cases, it is necessary for an SOE's company partners to identify where these conflicts lie and develop mitigation measures accordingly.

In some cases, an SOE's *de facto* roles will extend beyond its formal remit. Roles which SOEs often play include:

- ▶ commercial player, either as operator of assets or non-operating partner
- ▶ regulator, which could include the setting or enforcement of rules regarding operations, costs, health and safety, environmental and social obligations, or local content
- ▶ concessionaire, i.e., the entity that awards exploration or production licenses
- ▶ fiscal agent, as when the SOE collects or manages revenue streams on behalf of the state, including selling the state's share of production
- ▶ provider of public goods and services beyond the extractive sector
- ▶ commercial player outside the extractive sector.

Once a company identifies which roles the SOE plays, it should assess any existing or potential conflicts of interest and respond accordingly.

1.5. Assess the SOE's governance and accountability record against international standards.

In their due diligence, companies should examine how well the SOE does in meeting governance and accountability good practices. Gaps may represent important red flags, or areas where the partnership could aim to help improve on current practices.

As custodians of public resources, SOEs are held to different standards of governance and public accountability than privately-owned commercial entities. Several organizations including the Extractive Industries Transparency Initiative (EITI), NNGI, the OECD and the World Bank have published relevant guidance on SOE governance and anti-corruption standards.¹¹ Elements of the key standards are summarized below. This is not an exhaustive compilation, nor does it intend to replace the other sources of guidance. Rather, it highlights some of the standards most relevant to companies when they are assessing SOE corruption risks.

The SOE is transparent.

- ▶ The SOE meets all or most of the EITI Standard, an internationally recognized benchmark for SOE transparency.¹² The Resource Governance Index also includes relevant transparency indicators and allows comparisons of SOEs.¹³
- ▶ The SOE discloses up-to-date information on a consistent and regular basis, in an accessible format.
- ▶ While important, transparency is far from a perfect proxy for high integrity standards. Some SOEs, including Petrobras at the height of its corruption issues, have done well on transparency while falling short in controlling corruption.

The SOE is subject to effective oversight.

- ▶ The SOE has a professional and independent board which operates free from political influence. Other good board practices include having a majority of independent directors and a chair independent of government, and an audit committee with independent members and primary authority over the internal audit.
- ▶ It is clear which ministry or agency acts as the SOE's government shareholder, and there are clearly defined shareholder rights.

11 EITI, *The EITI Standard (2019)*; EITI, *Guidance on State-Owned Enterprises*; NNGI, *Resource Governance Index (2021)*; NNGI, *National Oil Company Database (2021)*; NNGI, *Guidance to Extractive Sector State-Owned Enterprise Declarations (2018)*; NNGI, *Natural Resource Benchmarking Framework (2016)*; NNGI, *Reforming National Oil Companies: Nine Recommendations (2014)*; OECD, *Guidelines on Anti-Corruption and Integrity in SOEs (2019)*; OECD, *Guidelines on Corporate Governance for SOEs (2015)*; World Bank, *Corporate Governance of SOEs: A Toolkit (2014)*.

12 EITI, *The EITI Standard (2019)*.

13 NNGI, *Resource Governance Index (2021)*.

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- ▶ The SOE is subject to regular, independent external audits.
- ▶ The legislature actively scrutinizes the SOE's performance and activities.
- ▶ The SOE engages with civil society, the public, the media and the business community, and critiques of the SOE do not prompt intimidation or retribution.

The SOE has robust integrity measures.¹⁴

- ▶ As above, the board has an independent, active and capable audit committee.
- ▶ The SOE has robust anticorruption policies and practices (covering risk areas such as due diligence procedures, political and charitable payments, gifts and hospitality), an actively implemented code of conduct and a whistleblowing mechanism.
- ▶ Law or SOE policy require board members and management to disclose their assets, and they do so. They are also prohibited from holding commercial interests in the sector.
- ▶ When credible corruption allegations arise, the SOE or the relevant authorities take action and respect due process for investigations and prosecutions.
- ▶ The SOE implements robust risk-based due diligence in its procurement—e.g., it collects beneficial ownership information and screens third parties for corruption risks.

The SOE supports fair competition in the sector.

- ▶ When the SOE awards business opportunities, including licenses, equity shares, trading contracts or supply contracts, the award process is transparent, in compliance with local laws and regulations, and free from political interference. It also uses an open tender when feasible.
- ▶ SOEs do not require or encourage the use of agents to participate in tenders.
- ▶ The SOE implements any local content programs in a manner free from political bias and that avoids conflicts of interest.

1.6. Strengthen due diligence practices for short-term transactions with SOEs and when SOEs are clients.

As noted, companies often do not conduct elevated due diligence on SOEs when they are seeking smaller contracts or trading opportunities from the SOE. Because these engagements are often shorter-term, relatively standardized and require less in-country presence, companies often have less motivation, leverage and time to devote to due diligence.

However, companies engaged in these types of deals can still enable corruption, and should conduct enhanced due diligence on their SOE clients to avoid doing harm.

¹⁴ See, in particular, OECD, *Guidelines on Anti-Corruption and Integrity in SOEs (2019)*.

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Companies have adopted several good practices in this scenario:

- ▶ Make the avoidance of enabling corruption and causing societal harm explicit aims of the due diligence process, even when due diligence is more abbreviated.
- ▶ Conduct and keep on file enhanced counterparty due diligence on SOEs from which a company frequently seeks business. Companies should update this regularly and make sure it feeds into decisions around individual transactions.
- ▶ Vet the tender itself and similar ones. Examine the agenda it serves. Is it a vehicle for patronage, self-enrichment or other problematic outcomes? Conduct enhanced due diligence and escalate decisions around whether to participate in awards that exhibit flaws or deviations from commercial standards, or avoid them altogether. Such deviations could include rushed timelines, lenient terms, absence of competition where it would typically exist, past records of abuse or bias, or missing documentation and procedures.
- ▶ Conduct enhanced due diligence on other parties related to the transaction, and strictly avoid transactions where these parties have red flags. Examples could include advisors hired by an SOE to manage an infrastructure tender, or intermediaries in a trading transaction.
- ▶ Adopt the payment control measures proposed in Section 4 to safeguard against misappropriation.
- ▶ Establish and publicly disclose red lines that reflect the company's risk tolerance for counterparties, such as those proposed in Recommendation 3.2. Up-front safeguards of this kind may be even more important for companies making lower investments in compliance.
- ▶ If a company lacks the resources to vet every transaction, it may need to avoid doing business where corruption risks run high.

2. Avoiding high-risk agents

The challenge

Agents feature commonly in corruption schemes in the extractive sector and beyond, including in transactions involving state-owned enterprises (SOEs). While definitions vary, the term “agent” typically refers to third-party individuals or organizations that represent a company or act on its behalf. An analysis of 427 foreign bribery cases conducted by the OECD found that three quarters involved different types of intermediary, including agents.¹⁵ This trend is widely evident in the oil and mining industries: NRCI identified more than 30 prominent recent cases that involved the use of agents of various forms, including these well-known examples:

- ▶ Investigations have revealed that Unaoil paid bribes in at least nine countries while serving as an agent for several major oilfield service companies. The firm’s clients included SBM Offshore, which paid USD 238 million to settle charges of bribery of SOE officials to win contracts in Brazil, Angola, Equatorial Guinea, Kazakhstan and Iraq,¹⁶ and TechnipFMC, which agreed a USD 296 million criminal settlement for bribery of SOE officials in Iraq via Unaoil, among other charges.¹⁷
- ▶ A former employee of Gunvor, a commodity trading firm, routed bribes through a network

15 OECD, *OECD Foreign Bribery Report. An Analysis of the Crime of Bribery of Foreign Public Officials* (2014).

16 U.S. District Court for the Southern District of Texas. *United States vs. SBM Offshore N.V., Deferred Prosecution Agreement. Criminal No.17-686*. 29 November 2017.

17 U.S. District Court for the Eastern District of New York. *United States vs TechnipFMC plc. Deferred Prosecution Agreement*. Case Number 19-CR-278. 25 June 2019.

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of intermediary companies to help Guvnor win oil-trading contracts from the Republic of Congo's national oil company.¹⁸ In 2019, Gunvor agreed to a USD 95 million criminal penalty with Swiss authorities over these bribes and others in Côte d'Ivoire.¹⁹ The U.S. Department of Justice and Office of the Attorney General in Switzerland have also opened investigations into allegations that Gunvor used bribes to win business from the Ecuadorian national oil company between 2012 and 2020. Similarly, this allegedly involved the use of agents.²⁰

- ▶ An estimated USD 2 billion was lost to corruption in the “Car Wash” scandal which centered around the Brazilian state oil company, Petrobras, between 2004 and 2012. U.S. Department of Justice case files show that intermediaries played a critical role in channeling corrupt proceeds between contractors, traders, SOE and government officials, and political party personnel in Brazil.²¹

Due in part to cases such as these, many companies have taken important steps to reduce the corruption risks posed by agents. Several have committed to stop using agents when seeking new business, while others have significantly reduced their use of agents.²² Many companies have strengthened the due diligence and oversight mechanisms that apply to agents. Some governments and SOEs are also changing their practices—for example, by reducing the agent requirements for companies seeking to participate in their licensing and procurement systems.²³

Despite these changes, companies continue to use agents to help secure various licenses and contracts in countries around the world. Their use varies widely. Several large international oil companies report no longer using agents in their exploration and production business as their economic clout and global reach allow them to engage directly with SOEs and governments. However, smaller producers still rely on agent services. Some larger commodity traders have reportedly discontinued the use of agents, while others use them in certain jurisdictions. In the services segment of the industry, agents remain prevalent, helping service companies identify opportunities and navigate tenders. In some countries, the use of agents is still required or expected by the SOE or the relevant authorities, in some cases as part of local content

18 Andy Hoffman and Hugo Miller. “*Trader Gunvor Pays \$95 Million to Swiss in Corruption Probe.*” Bloomberg, 17 October 2019; Ministère Public de la Confédération Suisse. “*Press release: Le négociant en matières premières Gunvor condamné pour responsabilité pénale en lien avec des actes de corruption.*” 17 October 2019.

19 Hoffman and Miller.

20 Andy Hoffman. “*New Gunvor Bribery ‘Skeleton’ Haunts Oil Trader’s Reform Pledge.*” Bloomberg, 7 April 2021; U.S. District Court for the Eastern District of New York. *United States vs. Raymond Kohut*. Criminal Number 21-115. 6 April 2021; Office of the Attorney General of Switzerland. “*Press release: Oil trading in Ecuador: Office of the Attorney General of Switzerland opens investigation.*” 30 June 2021.

21 U.S. Department of Justice. *Petrobras Non-Prosecution Agreement and Statement of Facts*. 26 September 2018.

22 Gunvor Group Limited. “*Press release: Gunvor to Cease Use of ‘Agents.’*” 18 November 2020; Neil Hume, “*Trafigura Ends Use of Middlemen After Corruption Probes.*” Financial Times, 14 July 2019.

23 For instance, the Abu Dhabi National Oil Company’s “*General Terms and Conditions for the Sale of Crude Oil/Condensate and Liquefied Petroleum Gas.*” January 2021, strictly limits company use of agents in acquiring oil trading contracts.

requirements. Several companies expressed frustration that the high-risk countries where they would most prefer to avoid working with agents are the very same markets where the authorities expect them to do so.

This diversity of practice reflects changing market conditions and the absence of industry standards around the use of agents—a gap which the following recommendations could help to fix. Some of the proposals below reflect the rapid changes already observed in this area, while others represent more forward-looking measures to address these proven risks.

Recommendations

The following recommendations apply to the use of agents by several types of extractive sector companies, including those involved in oil, gas and mineral exploration and production; commodity traders; and service companies. As noted above, the term “agent” typically refers to the third-party individuals or organizations that represent a company or act on its behalf. Many different third parties can play this type of role, including intermediaries, consultants, law firms, accountants and local equity partners.

2. Companies should eliminate or reduce the use of business development agents, and stop agent practices which exacerbate corruption risks.

Specifically, companies should:

2.1. Use a functional approach to identify the company’s high-risk agents.

One challenge to advancing industry standards on agents is being clear about which types of actor and role the term covers. There are various definitions of “agent” in circulation in the industry, and a wide range of actors undertake agent-like functions. Some company interviewees indicated how these definitional and labelling challenges can cause confusion and obscure where the real risks lie. Companies should therefore identify and manage agents according to the functions they fulfil.

Past corruption cases and current company practices suggest the following useful distinctions:

Business development or operational agents

The first distinction concerns the timing of the engagement. Companies hire business development agents to support the identification and acquisition of new business. Companies may refer to representative business development agents as commercial, sales, marketing or origination agents,

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and they widely recognize these as among their highest-risk third-party relationships.

Companies also hire agents to support operational approvals and processes, after the business has been won. These agents, such as customs and ports agents, can also carry high corruption risks.²⁴

Representative or advisory functions

Agents serve different functions, including representative or advisory functions. Representative functions occur when an agent pursues the company's interests with an SOE or relevant government officials, while advisory functions are a more typical form of service delivery. Some entities perform both.

Representative functions may include:

- ▶ sourcing or identifying new business opportunities
- ▶ making introductions to key actors in a market
- ▶ negotiating on a company's behalf
- ▶ acquiring information on a company's behalf
- ▶ helping to secure project approvals or operational permits
- ▶ carrying out other SOE- or government-facing activities, even if the agent is not formally empowered to act on the company's behalf.

Advisory functions include:

- ▶ supplying market intelligence or advice on a transaction
- ▶ providing legal and accounting services, such as analysis of the country's legal framework
- ▶ giving local start-up support, such as establishing an office or forming a local company
- ▶ delivering operational support, such as interpretation, logistics, customs and immigration services.

No category of agent is risk-free, as past corruption cases clearly show. However, the recommendations below reflect the differing risk profiles across these groupings. Some recommendations focus on representative business development agents, given the high-stake risks they often pose. Conducting a functional mapping can help companies take a more differentiated approach to entities that play agent roles. Information on all agents should be collected in a centralized database which clarifies their functions and the risk level they are assigned.

²⁴ For more on managing operational agent risks, see Peter Wilkinson, *Managing Third Party Risk: Only as Strong as Your Weakest Link*, Transparency International U.K. (2016); World Economic Forum, *Good Practice Guidelines on Conducting Third-Party Due Diligence* (2013).

2.2. Take steps to eliminate the use of representative business development agents.

Drawing on their mapping of agents and agent functions, companies should take steps to eliminate the use of business development agents. In doing so, they should be alert to advisory agents that end up providing representative services, and work to eliminate these practices as well.

Eliminating representative business development agents is an increasingly common practice in the industry, and is a reasonable response to the frequent appearance of agents in recent corruption cases. However, not all companies will choose to take this step. Companies that continue to hire business development agents, particularly in the services sector, should seek to minimize their use overall, avoid agents when seeking business in high-risk contexts, and adopt the recommendations below. NRCI's interviews indicate many of these measures represent widely adopted good practices.

These recommendations come with important caveats. As companies reduce their use of agents, employees or other third parties may pick up the high-risk functions, including in business development. As one interviewee commented, "Someone still needs to open the door for them." Company personnel may engage in bribery or other inappropriate behavior, motivated by strong incentives to bring home a deal or move a project forward. Corruption schemes are often "co-created" and collaborative in nature, with employees orchestrating the scheme and using agents as the implementing tool. Alternatively, other third parties may pick up agent functions and act as "quasi-agents," including types of third party not subject to heightened anticorruption controls. For instance, an entity providing legal, tax or accounting advice could also offer representative functions with notable corruption risks. Companies must be alert to the unintended consequences of reducing agent use and prevent corruption in high-risk activities undertaken by their own personnel or other third parties.

2.3. Publicly commit to restrictions around working with certain types of agent.

Companies should commit up front to eliminating agents which, through due diligence, are shown to exhibit red flags on a predetermined list. Clear rules that prohibit inappropriate types of third party can ensure consistency in decision-making and reduce the number of *ad hoc* judgment calls that company employees must make when pressures to advance a deal run high. Companies should adopt rules against engaging with:

- ▶ entities that will not report their beneficial owners
- ▶ entities whose key personnel or beneficial owners include:

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- ▶ a public official with a conflict of interest relating to the business the company is seeking²⁵
- ▶ a former official who recently left such a position of influence, for example, within the last 24 months²⁶
- ▶ individuals in violation of the producer country's prohibitions on public officials acquiring commercial interests²⁷
- ▶ individuals or entities convicted or otherwise credibly shown to have engaged in corruption-related offenses, and where evidence of adequate remediation is not found.

2.4. Apply special controls and scrutiny to any remaining agent relationships.

Agents that remain on a company's books require special scrutiny and monitoring. If an agent is needed, the company should adopt controls including those outlined below. This is not an exhaustive list, but represents leading ideas drawn from existing company good practice and resources such as Transparency International's guidance on third-party risk management.²⁸ These controls should apply to all agents but are particularly important for those with representative functions.

- ▶ **Justification.** The company should require the commercial team hiring the agent to provide to the compliance team or another appropriate body a case-by-case justification for the legitimate and unavoidable need for the agent's use. The questionnaire used to secure this information could ask about how the agent was identified, why it is required to engage them, why existing internal teams or third parties cannot provide the same services, and how the agent will be remunerated. This justification should be secured regularly (e.g., annually) for long-standing arrangements.
- ▶ **Due diligence.** Due diligence on agents should include obtaining and verifying beneficial ownership information; screening for political exposure and potential harms (see Recommendation 3.5) and conflicts of interest (including through fiduciary obligations); checking sanctions and watchlists; examining how they obtained their agent designation from the

25 The OECD defines a conflict of interest as "a conflict between the public duty and private interests of a public official, in which the public official has private-capacity interests which could improperly influence the performance of their official duties and responsibilities." Conflicts in this context can take many forms, most seriously when an official holds decision-making power or has access to inside information concerning the business a company is seeking. OECD, "[Recommendation of the Council on OECD Guidelines for Managing Conflict of Interest in the Public Service](#)," OECD/LE-GAL/0316. 28 May 2003.

26 This recommendation does not mean conflicts of interest end after this period. As the Financial Action Task Force (FATF) notes, "The handling of a client who is no longer entrusted with a prominent public function should be based on an assessment of risk and not on prescribed time limits." FATF, [FATF Guidance: Politically Exposed Persons \(Recommendations 12 and 22\)](#) (2013).

27 NRGi reviewed over 50 mining and oil laws and found that about half contained prohibitions on PEPs holding interests in the sector. Erica Westenberg and Aaron Sayne, [Beneficial Ownership Screening: Practical Measures to Reduce Corruption Risks in Extractives Licensing](#), NRGi (2018).

28 On agents and intermediaries see Transparency International U.K. [Global Anti-Bribery Guidance](#) (accessed 8 December 2021); Transparency International U.K., [Defence Companies Index: DCI Indicators](#) (accessed 8 December 2021).

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SOE or government (if applicable); and assessing the agent's qualifications, compliance systems, reputation and references. Companies reported that face-to-face meetings, ideally at the agent's office, are one effective method for identifying red flags and communicating expectations during this process. The due diligence should be repeated regularly for longstanding agents.

- ▶ **Scrutiny.** Companies should require:
 - ▶ multiple staff from different departments to participate in agent due diligence, selection, contracting and payment approvals. Some companies have established committees for this purpose.
 - ▶ an employee to take clear responsibility for the agent relationship (including justifying their use, the due diligence, contracting and oversight).
 - ▶ written documentation of communications with prospective and current agents related to contracts and interactions with government and SOE officials.
 - ▶ regular reports from the agent on the services provided, particularly in the case of agents working on a retainer.
 - ▶ company staff to approve in advance and attend all meetings between agents and government or SOE officials, particularly in the case of business development agents.
 - ▶ annual certification that the agent complies with the company's anticorruption measures.
 - ▶ maintenance of an up-to-date list of all agents, with details on the related end-customers and projects, names of the responsible points of contact, sales amounts, the agent's commission or fees, and the basis for their calculation.
 - ▶ regular internal audits focused on high-risk agent relationships, which can involve a review of documents (transaction testing) and interviews with the agent's representatives.

- ▶ **Contract obligations.** Contracts with agents should include:
 - ▶ the agreement of clear, time-bound deliverables which can be tracked and tied to payments, and the use of payment terms which do not incentivize corruption. (See 2.5 below.) Companies should avoid evergreen contracts that automatically renew in favor of contracts tied to the provision of specific services during a specified time period.
 - ▶ provisions that oblige the agent to follow the company's anti-corruption and ethics policies and complete compliance training.
 - ▶ a requirement that agents submit regular written updates of their activities, including written minutes of all interactions with government and SOE officials.
 - ▶ a requirement to report any suspected integrity concerns through dedicated "speak-up" channels (whistleblowing or complaints lines).

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- ▶ provisions that give the company the legal right to learn of any change in ownership or control of the agent, or any fiduciary duties to another party; sign off on any subcontracting of the agreed work, and require the subcontractor to follow the same rules; audit the agent's activities, including business integrity audits; and terminate the contract at its convenience (not just in case of a breach).
- ▶ **Payment controls** as covered in 2.6 below.
- ▶ **In-house safeguards.** As noted above, reducing the use of agents will require company employees to perform additional high-risk activities. Several companies reported strengthening internal controls with this challenge in mind, which may include adapting and applying some of the measures recommended here.

2.5. Publicly disclose the company's agent policy, a list of its agents and, over time, their beneficial owners.

Given the widespread concern about corruption in this area, companies should publish the policy that governs their use of agents.²⁹ The policy should be sufficiently detailed for an outsider to understand the company's approach and should reflect many of the recommendations suggested here—including the up-front commitment not to work with agents with certain attributes (as proposed in 2.2 above). Where companies continue to work with agents, they could identify the relevant jurisdictions and the categories of activity for which they use agents. This information could form part of the company's wider anticorruption policy and apply to all divisions, including subsidiaries and joint ventures. Several companies have published information about changes to their agent policy, suggesting that external stakeholders value information about how companies are handling this known area of risk.³⁰

Companies should also publish a list of their agents and basic information about the purpose, location and timeline of their work. While the disclosure of all agents is preferable, the list should at least include all representative business development agents. Public reporting is a proactive anticorruption measure which should be utilized in the sector's most corruption-prone areas. Disclosures would discourage problematic actors from engaging with the company and demonstrate the company's commitment to integrity.

29 Many companies already do this, but several do not. NRCI reviewed the publicly available policies of 25 large extractive companies and found that 13 (52 percent) disclosed some information on their approach to managing agents, although the level of detail provided is generally very limited (information accurate as at November 2020). Some examples of published policies include ENI SpA, "[Management System Guideline Anti-Corruption](#)" (2021); Total S.A., "[Business Integrity Guide](#)" (2015) and ExxonMobil Corporation, "[Anti-Corruption Legal Compliance Guide](#)" (2014).

30 See Gunvor Group Limited. "[Press release: Gunvor to Cease Use of Agents](#)," 18 November 2020; Trafigura Group Pte. Ltd. "[Press Release: Statement on the Company's Decision re the Use of Third Parties for Business Development](#)," 15 July 2019.

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Companies should publicly disclose the beneficial owners of their agents, or require that their agents disclose this information. Beneficial ownership transparency constitutes a growing approach to preventing conflicts of interest and other corruption risks.³¹ Such a measure has also been recommended for the defense sector, where agents have similarly featured in many corruption cases.³² If this policy is not feasible to implement in full, companies could focus on agents with the riskiest functions, larger agent contracts or high-risk jurisdictions. This reporting would likely entail revisiting legal terms with existing agents. As an interim measure, companies could encourage their agents to disclose their true owners—for example, by asking agents to indicate during the due diligence or application processes whether they disclose their beneficial owners; favoring beneficial ownership disclosure in agent tenders, and providing guidance on disclosure. For more on third-party beneficial ownership transparency, see Recommendation 3.4.

2.6. Adopt payment structures which discourage corruption, including avoiding success fees.

How an agent is paid can impact the incentives and possibilities for corruption. The safest model is to link payment directly to the provision of agreed services, and pay for those services after they are provided. Business development agents would therefore be paid even if the company is unsuccessful in securing the business. The amount of the payment should not exceed local industry rates for the services in question or, where local rates do not exist, those consistent with international practice and the scope of service. Companies may want to establish maximum values for agent remuneration.

Success fees and commissions are frequently used in the extractive industries and carry the highest corruption risks. Success fees arose to align the incentives of the agent with their clients, with both parties motivated to bring home the deal. In practice, they have increased incentives for corruption, encouraged a “win at any cost” mentality, motivated cost inflation and played a role in several corruption cases involving agents. Retainer fees and mobilization fees also carry higher risks when not linked to the provision of specific services.

Given the record in this area, companies should publicly commit in their agent policy to eliminating success fees, commissions and other incentive-based pay (or explaining their

31 In September 2021, a group of six companies (AngloAmerican, BHP, Glencore, Newmont, Repsol and Rio Tinto) issued a statement endorsing beneficial ownership transparency. EITI. “[Statement by companies on beneficial ownership transparency.](#)” August 2021. See also Alexandra Gillies, “[Leading Companies Issue Commitments on Beneficial Ownership: Will It Help Prevent Corruption?](#)” NRCI, 10 September 2021.

32 Transparency International U.K., [Defence Companies Index: DCI Indicators](#) (accessed 8 December 2021).

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continued and preferably limited use), and move to linking payments to services as much as possible. Some companies have already taken this step. The collective action strategies noted below (see Recommendation 2.7) could help advance this cause in countries or industry segments that favor their use.

Along with avoiding high-risk payment types, companies should commit to basic financial controls (see Section 4), including only making payments into bank accounts held in the name of the contracted entity or individual; requiring multiple internal sign-offs on high-risk payments (from their legal or compliance and finance departments); avoiding payments to banks where there is evidence of weak anti-money laundering controls; reimbursing for a limited set of expenses in favor of paying allowances; requiring proof of performance documentation prior to making the payment, and prohibiting cash payments.

2.7. Explore opportunities for collective action.

Managing risks around agents is a challenge shared by companies in all segments of the industry, as well as governments and SOEs. Coordination among these actors could help to change long-established practices.

Pathways for collective action in this area include:

At the international level, industry actors could publicly commit to certain principles around agent use, including the measures noted above. Coordination of this kind can help reduce the commercial disadvantages to any one reforming company, and signal to agents and clients alike the importance of shifting away from past high-risk practices. Companies could agree to stop using certain risky fee types, publicly disclose their agents and their beneficial owners, or commit to red lines around certain agent functions. This form of action might be more viable within certain industry segments, such as among production, trading or service companies. It could also be organized with the support of industry associations.

At the country level, industry action might be most effective if undertaken jointly with specific governments or SOEs. For example, if a SOE requires the use of agents in a way that creates corruption risks, an appropriate authority or third party could help convene discussions about possible reforms. Goals could include reducing requirements to use agents, publishing a registry of approved agents, moving away from high-risk fees as a cost-control measure, or normalizing agent disclosure.

3. Responding to political exposure

The challenge

When due diligence screening of a third party identifies possible political exposure, companies must often make complex, subjective and context-specific decisions about how to respond. In particular, they must evaluate whether working with the party will constitute or enable corruption. These difficult decisions arise frequently with respect to the third parties that surround a company's engagement with SOEs, such as joint venture suppliers, local equity partners, trading intermediaries and other entities noted below. The following guidance aims to address this challenge, but could also apply to evaluation of politically exposed third parties unrelated to SOEs.

Past corruption cases reveal that companies, including publicly listed industry leaders, have facilitated corruption in producer countries by knowingly doing business with third parties with the following attributes:

- ▶ companies connected to politically exposed persons (PEPs) that acquired an exploration license or oil trading contract through a corrupt award process
- ▶ local companies widely known to be acting as proxies for top industry officials
- ▶ companies whose shareholders or beneficial owners were PEPs with no industry experience or other relevant capacity
- ▶ companies whose shareholders or beneficial owners were top officials in positions that created conflicts of interest, such as a senior SOE official
- ▶ companies owned by immediate family members or known proxies of a kleptocratic and authoritarian dictator, who had repeatedly received favorable access to business opportunities.

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For instance, in Angola, foreign companies partnered with several powerful PEPs despite their positions of influence and favored status.³³ In Nigeria, foreign companies did business with several local companies widely known to have received overly lucrative contracts thanks to their political connections, and with a former official who had benefited from a corrupt license award.³⁴ The U.S. hedge fund Och-Ziff and other firms partnered with entities owned by Dan Gertler in the Democratic Republic of Congo, despite being aware of his political connections and controversial past.³⁵ Often, in such instances, the politically exposed entity uses their standing to extract wealth from the country, which then contributes to wider patterns of elite enrichment at the public's expense. These practices inflict a heavy cost on the citizens of host countries, including lost revenues, operational delays, exacerbating the economic monopoly enjoyed by political elites, legitimizing kleptocratic actors, manipulating democratic processes and expanding the use of public office as an avenue for self-enrichment.

In other instances, companies have chosen to avoid or discontinue relationships with third parties that match these descriptions. The possible benefits of these decisions include avoiding anti-bribery investigations, protecting their reputations, upholding the company's ethical standards and not harming the countries where they work. Their choices suggest shifting norms and practices in the extractive industry. Risks that seemed acceptable a few years ago now look too serious to tolerate.

Companies aiming to avoid enabling corruption may face difficult choices, as their due diligence findings will not always point to obvious next steps. In some cases, working with politically exposed parties may be necessary. Their presence does not automatically signal corruption, but it does indicate the need for caution and careful analysis.

Past cases and company interviews indicate that the following factors complicate responses to political exposure:

- ▶ All qualified or approved companies for a certain service have PEPs among their owners.
- ▶ The service needed, such as market intelligence, requires the insider information and strong connections often most available to politically exposed parties.

33 Dmitry Zhdannikov and Julia Payne, "[Exclusive: Trafigura to Buy Angolan General's Stake in Puma Energy – sources.](#)" Reuters, 23 January 2020; Tom Burgis, "[Cobalt Cuts Ties with Two Angola Oil Partners.](#)" Financial Times, 28 August 2014; [Luanda Leaks](#) coverage, including Will Fitzgibbon, "[Isabel dos Santos Ordered to Return to Angola \\$500 Million in Shares 'Tainted by Illegality'.](#)" International Consortium of Investigative Journalists, 2 August 2021.

34 U.S. District Court for the Southern District of Texas, [Complaint, United States v. The M/Y Galactica Star](#). No. 4:17-cv-02166, 13 September 2021; Alexandra Gillies, Aaron Sayne and Christina Katsouris, [Inside NNPC Oil Sales: A Case for Reform in Nigeria](#), NRG (2015); Alexandra Gillies, [Crude Intentions. How Oil Corruption Contaminates the World](#) (New York: Oxford University Press, 2020); Sarah Kent and Eric Sylvers, "[Inside the Bribery Scandal Sweeping Through the Oil Industry.](#)" Wall Street Journal, 13 February 2018.

35 U.S. District Court for the Eastern District of New York. [United States vs Och-Ziff Capital Management Group LLC](#). Criminal No. 16-516. 29 September 2016; Franz Wild, Vernon Silver and William Clowes, "[Trouble in the Congo: The Misadventures of Glencore.](#)" Bloomberg, 16 November 2018.

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- ▶ Standard practice varies across countries, with industry players accepting politically exposed partners in one market that they would avoid elsewhere, due to factors such as lower perceived reputational risks, the small size of the local market, or the dominance of political elites in the local economy.
- ▶ SOE or government officials may pressure a company to accept a politically exposed partner.
- ▶ The information about political exposure is informal, unprovable or unreliable.
- ▶ The entity's ownership structure is opaque, e.g., it contains layers of offshore companies.
- ▶ Politically exposed entities appear lower down the supply chain, where the company has less influence or incentive to intervene, or the entities contract directly with the SOE but then work with the company.
- ▶ The entity's owners and beneficial owners do not show up as PEPs or show up as PEPs from a different sector, but they still exert control and receive benefits through proxies or informal channels.
- ▶ An entity's owners or key personnel include an individual who previously served as an official in a ministry, SOE or other relevant authority, making political exposure harder to assess.
- ▶ Large corruption cases implicated many industry players, leaving tough questions about who should be considered "rehabilitated."
- ▶ The company's commercial interests favor moving forward with an inappropriate party, and so it deems the corruption risks worth taking. Many corruption cases indicate that companies knew about the problematic status of their counterparty before deciding to move ahead.

Drawing on existing good practices and the analysis of past corruption cases, the following recommendations aim to help companies avoid enabling corruption or raising corruption risks via their third-party relationships. These steps will send the right signals to prospective third parties and other audiences about the company's priorities. They deploy transparency and up-front commitments as ways to reduce the number of *ad hoc*, high-pressure judgement calls that need to be made—scenarios that place staff in difficult positions and often feature temptations to accept risks rather than avoid them.

Recommendations

The following recommendations apply to the vetting of third parties by all types of extractive sector company, including exploration and production companies, commodity trading companies and service companies.

Common scenarios where they could be applied include the vetting of:

- ▶ minority equity partners
- ▶ suppliers and service providers
- ▶ agents and consultants (see also Section 2.)
- ▶ commodity trading intermediaries, e.g., companies that purchase or receive crude oil from a government or SOE and then sell it on to an international trader
- ▶ beneficiaries of social investment projects
- ▶ buyers of assets.

The recommendations apply to the vetting of third parties at the start of an engagement, as well as the regular evaluation of existing third parties. Many also apply to hiring decisions, including for temporary positions.

This guidance assumes that companies are gathering robust information as part of their due diligence process, including making use of different resources to identify and assess third-party political exposure. Some companies rely heavily on PEP databases, particularly for high-volume transactions such as oil trades. These databases are valuable, but they may miss some risky actors and do not shed light on the implications of political connections. The review of public records, local knowledge of company employees, and reports prepared by independent external providers can all help fill this gap.

3. Companies should screen out politically exposed third parties who may cause harm to producer countries, and should publicly commit to avoiding inappropriate partners.

Towards this end, companies should:

3.1. Adopt a robust definition of politically exposed persons in the company's anticorruption policies, and commit to conducting enhanced due diligence on third parties that meet this definition.

The PEP definitions that companies publish are currently too limited in most cases. NRCI reviewed the published policies of 25 large extractive industry companies. The majority (15) include government officials in their definition of PEPs, which in all cases covers SOE officials. However, less than half (11) explicitly refer to the risks around officials' family members, and only three refer to risks around their close associates.³⁶ Internal procedural documents may contain broader definitions, but these do not inform the public or send the right signals to external stakeholders.

The Financial Action Task Force (FATF) recommends enhanced scrutiny of individuals entrusted with prominent public functions, as well as their family members and close associates.³⁷ Companies should adopt a definition which includes these different relationships because they reflect risk patterns widely apparent in the industry. It is also important to consider that political elites may exercise influence even when they do not formally hold a public role, and political exposure is also present at different tiers of government, including subnational officials.

Along with publishing a robust PEP definition, companies should publicly commit to requiring senior manager approval and conducting enhanced due diligence on entities whose personnel or beneficial owners fall into this category. This should include adequate measures to assess that the person's overall wealth in addition to the funds involved in the related business are derived from legitimate sources.³⁸ While this section focuses on third parties, a company should also use a strong PEP definition and other measures recommended here in its recruitment and screening of personnel.

3.2. Publicly commit to restrictions against working with certain types of entities.

While the diversity of operating contexts does call for a flexible approach, it is possible for companies to designate certain no-go areas in their partnerships. These restrictions will not cover all inappropriate parties, and therefore entities that meet this basic test will still require further due diligence and review. At a minimum, companies should commit up front, in their public anticorruption policy, that they will not work with:

- ▶ entities that will not report their beneficial owners
- ▶ entities whose key personnel or beneficial owners include:

³⁶ Company policy review conducted in November 2020. Information accurate at this date.

³⁷ Financial Action Task Force (FATF), *FATF Guidance: Politically Exposed Persons (Recommendations 12 and 22)*, (2013).

³⁸ This reflects guidance from FATF (ibid) and from the U.K. Financial Conduct Authority, *FG 17/6 The Treatment of Politically Exposed Persons for Anti-Money Laundering Purposes* (2017).

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- ▶ a public official with a conflict of interest relating to the business the company is seeking³⁹
- ▶ a former official who recently left such a position of influence, for example, within the last 24 months⁴⁰
- ▶ individuals in violation of the producer country's prohibitions on public officials acquiring commercial interests⁴¹
- ▶ individuals or entities convicted or otherwise credibly shown to have engaged in corruption-related offenses, and where evidence of adequate remediation is not found.

It is worth noting here that due diligence research often fails to uncover definitive evidence. Companies should therefore not work with an entity where there is a reasonable basis to believe that any of these scenarios apply.

Committing to these basic restrictions publicly and up front may in some circumstances limit a company's flexibility and capacity to make context-specific decisions, a concern that several companies expressed. However, past corruption cases indicate that universal case-by-case discretion has not adequately protected the public interest. Adopting these basic prohibitions could help avoid harmful incidents. There should be very few instances in which third parties matching these descriptions represent advisable partners.

Adopting and communicating these measures would inform prospective partners and other external stakeholders about the company's standards, and could strengthen its negotiating position when it feels pressure to take on an inappropriate partner. The commitments would also reduce the number of scenarios when staff must make discretionary decisions, and discourage against these standards being abandoned when the pressure to close a lucrative deal runs high. As one company representative explained, "We need rules that require people to make the right choices, and [do] not put staff in a position where they have to be whistleblowers and take on a giant company when concerns arise. Transparency can help solidify the processes and standards; it helps."

39 The OECD defines a conflict of interest as "a conflict between the public duty and private interests of a public official, in which the public official has private-capacity interests which could improperly influence the performance of their official duties and responsibilities." Conflicts in this context can take many forms, most seriously when an official holds decision-making power or has access to inside information concerning the business a company is seeking. OECD, "[Recommendation of the Council on OECD Guidelines for Managing Conflict of Interest in the Public Service](#)," OECD/LEGAL/0316. 28 May 2003.

40 This recommendation does not mean conflicts of interest end after this period. As the Financial Action Task Force (FATF) notes, "The handling of a client who is no longer entrusted with a prominent public function should be based on an assessment of risk and not on prescribed time limits." FATF, [FATF Guidance: Politically Exposed Persons \(Recommendations 12 and 22\)](#), (2013).

41 NRG I reviewed over 50 mining and oil laws and found that about half contained prohibitions on PEPs holding interests in the sector. Erica Westenberg and Aaron Sayne, [Beneficial Ownership Screening: Practical Measures to Reduce Corruption Risks in Extractives Licensing](#), NRG I (2018).

3.3. Require all third parties to submit beneficial ownership information, and work to verify this information for high-risk parties or transactions.

Beneficial ownership reporting represents a necessary and practical step towards addressing this challenging area of compliance. It sends the right signals to internal and external stakeholders, including prospective third parties. Thanks to significant global momentum and emerging company practice, there are ample definitions, precedent and guidance available.⁴² Although beneficial ownership reporting cannot replace risk-based due diligence, not least because beneficiaries can be readily hidden, it represents an important practical tool for extractive sector companies.

Companies need to first disclose their own beneficial owners in accordance with recognized best practice and open data standards.⁴³ They should then require that all third parties report their beneficial ownership information, as part of due diligence and prior to contracting, and publicly disclose this policy. If an entity is unwilling to provide the information, the company should not do business with it, and if the information turns out to be false, the business should be ended. Several companies already follow this simple rule and report it as useful and feasible.⁴⁴ This approach is also viable for high-volume transactions, such as crude oil spot sales.

To implement this measure, companies could add a beneficial ownership field to the forms they ask prospective vendors to complete, and arrange a similar mechanism for unpaid counterparties such as clients or joint venture (JV) partners. Setting an ownership threshold for this reporting is a tough choice, but there is guidance available on this question.⁴⁵ Publicly listed entities could provide a link to the relevant stock exchange filings.

Companies should then invest in verifying the beneficial ownership information provided in high-risk transactions, which reflects existing good practice.⁴⁶ Some company representatives have expressed concern about sending their staff on unending “treasure hunts” for beneficial ownership information. Asking suppliers to self-report should help lessen this task, with the efforts at verification steered towards high-risk and large-scale deals.

42 See, for example, the U.K. corporate registry, the EITI's beneficial ownership reporting requirements in *The EITI Standard (2019)* and Open Ownership, *The Open Ownership Principles*, (2021).

43 Open Ownership, *The Open Ownership Principles*, (2021). The 2019 EITI Standard and the Global Reporting Initiative standard for the oil and gas sector (*GR-II*, effective on or after 1 January 2023) set out complementary standards for transparency in company ownership. Publicly listed companies, including wholly owned subsidiaries, should publish a link to the stock exchange filings where they are listed.

44 In 2021, six large extractive companies committed to several measures to advance beneficial ownership reporting that align, to some degree, with these recommendations. EITI, *Statement by companies on beneficial ownership transparency* (2021). NRGi published a review of the commitments and advice on how they can help prevent corruption. Alexandra Gillies, *Leading Companies Issue Commitments on Beneficial Ownership: Will It Help Prevent Corruption?* (2021).

45 Open Ownership, *Beneficial Ownership in Law: Definitions and Thresholds* (2020).

46 Cari Votava, Jeanne Hauch and Francesco Clementucci, *License to Drill: A Manual on Integrity Due Diligence for Licensing in Extractive Sectors*, The World Bank (2018); Transparency International U.K., *Global Anti-Bribery Guidance* (accessed 8 December 2021).

3.4. Move toward the public reporting of beneficial ownership information for joint venture partners, large suppliers and high-risk third parties.

The trend towards beneficial ownership transparency is clear and companies can play an important role in spreading this practice across the sector. Rio Tinto and Glencore already publish ownership information for their JV partners.⁴⁷ These companies, as well as AngloAmerican, BHP, Newmont and Repsol, committed in 2021 to disclosing beneficial ownership information for equity partners (or disclosing why they cannot) and to “encouraging other companies, including joint venture partners, contractors and suppliers, to publicly disclose their beneficial owners.”⁴⁸ Since January 2020, the 55 countries that implement the Extractive Industries Transparency Initiative (EITI) have been required to publicly disclose beneficial ownership information for all companies that apply for or hold exploration or production licenses. Outside the sector, 110 countries have committed to advancing beneficial ownership registers, many of which will be publicly available.⁴⁹

It will take many years until governments establish national registers of ownership information across resource-rich countries and other relevant jurisdictions. Companies have an important role to play during the interim period to encourage transparency in the highest-risk parts of the extractive industries. Several companies expressed concerns that ownership information could be seen as commercially sensitive and may infringe on partners’ privacy. The reporting may also entail costs, such as having to revisit legal terms with partners. However, the benefits to companies and the public would make such costs worthwhile.⁵⁰ Such gains include lowering corruption and fraud risks, facilitating due diligence and contributing to a more open and accountable extractive sector.

Public disclosure is an inexpensive and effective way to guard against false or incomplete beneficial ownership reporting, and signals a company’s commitment to integrity. The company could take a phased approach and begin with requiring beneficial ownership transparency from its largest and highest-risk partners, whose beneficial owners it should already know. These could include:

- ▶ JV partners
- ▶ major suppliers, above a threshold appropriate for the project and host country
- ▶ highest-risk third parties, such as business development agents (see Recommendation 2.5), partners on social investment projects and commodity trading intermediaries.

47 Rio Tinto, [Joint Venture Beneficial Ownership](#), 1 August 2021; Glencore Plc., [Joint Venture Beneficial Ownership 2021](#) (accessed 8 December 2021).

48 EITI, “[Statement by companies on beneficial ownership transparency](#)” (2021).

49 Open Ownership, [Worldwide Commitments and Action](#) (accessed 8 December 2021); Theo Van der Merwe, [Beneficial Ownership Registers: Progress to Date](#), U4 (8 April 2020).

50 For more on the business case for beneficial ownership transparency, see Daniel Hart, May Miller-Dawkins and Lida Preyama, [Putting Beneficial Ownership Transparency into Practice](#), B20 (2015).

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As an interim measure, companies could encourage third parties to disclose their true owners—for example, by asking them during the due diligence and contracting processes to indicate whether they disclose their beneficial owners, assessing beneficial ownership disclosure in third party tenders, and providing guidance on disclosure.

3.5. Evaluate engagements with politically exposed third parties for their risk of enabling corruption, and avoid engagements that carry those risks.

In some instances, companies enable corruption when they do business with politically exposed entities, by directly or indirectly helping corruption take place. Companies can enable specific corrupt transactions or more systemic forms of corruption. The latter refers to the conditions present in many countries where powerful groups have rigged the extractive sector to suit their narrow interests, at the expense of citizens. Systemic corruption is typically propagated by those who hold political power, and is often “legal” as those in power shape rules and laws to suit their own interests.

Companies should avoid enabling corruption, to minimize their own reputational and commercial risks, and to help prevent the societal harms that corruption causes. Particularly in its systemic forms, corruption can cause host countries to experience lost public revenues, reduced competitiveness and sector performance, reduced investor confidence, environmental damage, harms to host communities, economic stagnation, entrenchment of corrupt monopolies, weakened democracy, loss of public faith in state institutions, unrest and conflict.⁵¹

The idea that companies should guard against indirectly contributing to societal harm has received more attention in the area of human rights. The U.N. *Guiding Principles on Business and Human Rights* oblige companies to “prevent or mitigate adverse human rights impacts that are directly linked to their operations, products or services by their business relationships, even if they have not contributed to those impacts;” and, to conduct due diligence that covers this range of impacts.⁵² The U.N. Global Compact discusses different levels of corporate complicity in human rights abuses, all of which should be assessed and avoided.⁵³ The *OECD Guidelines for Multinational Enterprises* advise companies to “avoid causing or contributing to adverse human rights impacts” and to assess the potential for both direct and indirect human rights impacts as part of their due diligence systems.⁵⁴ There is growing recognition that corporate approaches to anticorruption and human rights converge in important ways,⁵⁵ though these two functions

51 On the costs of corruption, see, for instance: IMF, *Corruption: Costs and Mitigating Strategies* (2016); Alexandra Gillies, *Crude Intentions. How Oil Corruption Contaminates the World* (2020); United Nations Office on Drugs and Crime, *Effects of Corruption* (accessed 8 December 2021).

52 U.N. Human Rights Office of the High Commissioner (OHCHR), *Guiding Principles on Business and Human Rights*, OHCHR (2011).

53 U.N. Global Compact, *The Ten Principles of the UN Global Compact. Principle Two: Human Rights* (accessed 8 December 2021).

54 OECD, *OECD Guidelines for Multinational Enterprises* (2011).

55 For more discussion on the convergence of anti-corruption and human rights, see United Nations General Assembly,

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still operate separately within many extractive companies. As a practical step toward bridging this divide, companies should assess whether engaging with a politically exposed entity risks enabling corruption, and might therefore contribute to societal harms.

When due diligence reveals political exposure and when the third party does not fall into the categories of prohibited actors proposed in Recommendation 3.2 above, a company should assess whether doing business with the entity might lead it to enable corruption.

The following questions and illustrations could help guide this assessment. In many recent instances of companies enabling corruption, multiple questions would have applied.

Is the partnership likely to help political elites (or their proxies) unduly acquire wealth or otherwise benefit from the sector?

Scenarios where this has occurred:

- ▶ A company did business with an entity whose beneficial owners included a child of the country's president, even though that individual lacked experience or standing in the industry.
- ▶ A top industry official steered overly lucrative oil contracts to several proxy companies. Several international companies chose to do business with the proxy companies, despite knowledge of their affiliations. The proxy companies then spent some of the proceeds in ways that benefited the official.
- ▶ A company formed a JV with a local company owned by a powerful PEP and close presidential ally to access unique advantages in the market. The local partner received large returns from the business.
- ▶ A company hired a consultant with known ties to a top politician and decision-maker. The company paid the consultant a large fee, despite receiving few services other than introductions to key officials. The consultant then routed a portion of the funds to the politician.

Is the partnership likely to help a corruption scheme to function—for example, by providing access to financing, international markets or technical capacity?

Scenarios where this has occurred:

- ▶ An entity received an asset, supply contract or commodity through a corrupt award process and lacked the finances or qualifications to profit from the award, whether through operating a block, fulfilling supply obligations or marketing crude oil. The company engaged with the entity, enabling it to receive a financial return from the deal.

⁴A/HRC/44/43. Human Rights Council. *Connecting the Business and Human Rights and the Anti-Corruption Agendas*. Report of the Working Group on the Issue of Human Rights and Transnational Corporations and Other Business Enterprises," (2020); Joanna Drewert and Kaustuv Banerjee, *Linking Human Rights and Anti-Corruption Compliance*. U.N. Global Compact (2016); OECD and International Organization of Employers, *Connecting the Anti-Corruption and Human Rights Agendas: A Guide for Business and Employers' Organisations* (2020).

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- ▶ A company negotiated with an entity owned by a former official who acquired an extractive license through a corrupt process. The company then paid to acquire that license through a deal that enriches the former official, other middlemen and several officials.
- ▶ A company contracted for services or purchased commodities from an intermediary that served no commercial purpose, but instead was added into a deal solely to allow that intermediary to gain financially.

Is the deal likely to benefit a party that has received undue advantages thanks to their political position? Does their “source of wealth” indicate they represent and help replicate political and economic systems of favoritism and exclusion?⁵⁶

Scenarios where this has occurred:

- ▶ A member of a dictator’s immediate family received special access to economic opportunities during their career, and then partnered with foreign companies and service providers to earn further money and legitimize their position within global business circles.
- ▶ A company engaged third parties that were part of the businesses owned by several politically connected families that dominate the national economy and help to keep an authoritarian regime in power.

Is the partnership likely to create or worsen a conflict of interest? Is the prospective partner positioned to receive special treatment from an official, or will its involvement allow the company itself to receive special treatment?

Scenarios where this has occurred:

- ▶ The local partner in a JV was beneficially owned by a top SOE official who was able to influence procurement or regulatory decisions pertaining to the partnership.
- ▶ A company hired a supplier owned by a PEP with ties to extractive sector decision-makers. In some cases, the decision-makers were officials formally in charge of these matters. In others, they were politically powerful individuals who influenced them informally.
- ▶ A company formed a JV with a powerful PEP and received favorable access to a certain market.

While the above is intended to apply to suppliers, agents and other third parties, companies should perform a similar review as part of their due diligence of SOEs. (See Section 1.)

⁵⁶ This inquiry draws from the FATF’s important distinction between “expected” and “reasonably explained” wealth. Industry players often expect PEPs in certain countries will be rich, but that expectation does not mean the wealth is reasonable explained or legitimate. FATF, *FATF Guidance: Politically Exposed Persons (Recommendations 12 and 22)*, (2013).

4. Safeguarding payments

The challenge

In some countries, the funds paid by companies to state-owned enterprises (SOEs) could be used for illegitimate purposes. SOEs often play an important role in revenue collection; they receive production shares, contributions to operating expenses from non-operating joint venture partners, loans or payments for crude oil, among other types of payment. For many smaller SOEs, the payments received from international companies constitute most of the money they have on hand. Where there is weak accountability and poor governance, these payments may end up financing corruption.

Misappropriation and misuse of payments to SOEs are a serious problem. NRGi reviewed 21 corruption cases where illegal or illegitimate SOE spending took place, from countries in Asia, Africa, Eurasia and Latin America. Some of these diversions were clearly illegal, such as officials directly rerouting SOE funds into their private accounts. Others involved the allocation of funds for illegitimate purposes, such as spending on inflated contracts for politically connected companies or patronage-driven quasi-fiscal expenditure ahead of elections. While often legal, these transactions would fit common definitions of corruption.

The cases also vary by whether the payments are traceable. In some scenarios, officials direct or allow a particular payment from an individual company to be rerouted to private pockets. For instance, U.S. authorities allege that a top Republic of Congo official asked the SOE's bank to

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transfer the proceeds from a specific oil sale into his personal account, and then used the funds to purchase real estate and luxury goods. More often, the payments are fungible. In Brazil, when the SOE Petrobras paid inflated prices for services, as revealed in the “Car Wash” scandal, it was not possible to trace the original source of the funds.

It is tempting for companies to limit the scope of their due diligence and compliance, and look away from what happens after funds leave their accounts and enter those of an SOE. Yet the fate of these payments is still of concern. Companies have faced legal and reputational harms when SOEs or governments mismanage payments received. For instance, Equinor and BP faced regulator inquiry and negative media coverage concerning funds they paid to Sonangol in Angola to create a research center which for years failed to materialize. Shell and Eni faced prosecution after funds they paid to the Nigerian government were allegedly stolen. In neither case were the companies found guilty of any wrongdoing, but the investigations caused reputational harm. Banks and investors are also expressing greater concern about these matters.

Other prominent standards, such as the *OECD Guidelines for Multinational Enterprises*, call on companies to cease or prevent actions which may cause societal harms. Misappropriation diverts funds away from public goods such as healthcare and education, and into the pockets of a small number of private individuals. By attending to misappropriation risks, companies can avoid enabling harmful practices.

Although companies cannot control how SOEs manage and spend their funds (and nor should they), they can adopt measures to safeguard their payments to SOEs:

- ▶ Incorporate misappropriation risks into due diligence on SOEs, even for shorter-term transactions.
- ▶ Consistently apply financial controls to reduce immediate risks of diversion.
- ▶ Develop and stick to clear principles for responding to a reasonable belief that funds will be or are being diverted.
- ▶ Work with other stakeholders to help strengthen financial integrity.

Recommendations

This guidance applies to companies that transfer funds to SOEs, including companies engaged in the exploration and production of oil, gas and minerals, various types of joint venture partners, commodity traders and lenders to SOEs. Most of the recommendations apply to payments to other government entities as well.

4. Companies should actively protect against the misappropriation of payments made to SOEs.

Specifically, companies should:

4.1. Incorporate misappropriation risks in due diligence on SOEs, even for shorter-term transactions.

For transactions or partnerships with SOEs, companies' due diligence should explicitly consider misappropriation risks. While some companies have traditionally preferred to see these challenges as beyond their scope of concern, recent corruption cases and their fallout indicate the importance of systematically assessing this risk.

Risks of misappropriation are often foreseeable and depend in part on an SOE's history, its governance and its position in the wider political context. Section 1 of this guidance provides further recommendations on SOE due diligence, including a set of questions that companies can use to assess the seriousness of misappropriation risks and other forms of SOE corruption. (See Recommendation 1.2.)

For new engagements, companies can build mitigating controls into their contracts or consider avoiding the deal altogether. Embarking on project-based contracts as opposed to long-term framework agreements might also make exit more viable should concerns arise during the partnership. (See Recommendation 4.3 on responses to integrity issues.)

The box below lists red flags for misappropriation, which could inform this analysis.

Common warning signs of misappropriation

- ▶ The SOE withholds large portions of revenue otherwise due to the state, to the point that it pays the state far less than what is expected or legally required.
- ▶ The SOE claims the amounts withheld are to cover operating costs or improve its operational performance, but its debts are not met or its performance in these areas worsens over time.
- ▶ The SOE's explanations for its spending are vague or do not hold up to scrutiny—e.g., audits or third-party investigations cannot confirm them.
- ▶ The SOE spends heavily on items not in its designated or internal operating budgets.
- ▶ The SOE has a history of defaulting on debts, including when its revenues should be high.

- ▶ The SOE maintains an unusually high number of accounts, and payment flows do not follow predictable or legally mandated channels.
- ▶ The SOE withdraws or allows large sums to be withdrawn from its accounts in cash.
- ▶ Payment channels run through complex corporate structures, including offshore accounts.
- ▶ Available figures on the SOE's revenue flows and financial performance show serious gaps or discrepancies.
- ▶ SOE financial and spending decisions—especially contract awards—are routinely subject to high-level political interference.
- ▶ The SOE's quasi-fiscal expenditures benefit a particular political agenda or group.
- ▶ Foreign anticorruption legal actions implicate SOE officials in behavior related to misappropriation, but the SOE takes no action.

4.2. Adopt robust controls as a first line of defense against the diversion of payments.

The controls listed below reflect company practices and existing guidance on financial controls.⁵⁷ Many will be familiar to companies, but it is critical they achieve consistency in applying these controls, regardless of commercial pressures.

Companies should:

- ▶ require “several pairs of eyes” from different departments, including senior personnel, to scrutinize and sign off on payments to SOEs, and designate an individual with responsibility for the transaction, to ensure accountability.
- ▶ ensure heightened scrutiny of SOE transactions by the internal audit function, and oversight of SOE payments by the audit committee.
- ▶ verify that an SOE has the legal right to collect the payment, and that it secured all required governmental approvals for the transaction.
- ▶ confirm that the bank account is held by a corporate entity controlled by the SOE and is designated for collecting the revenue in question, and that the authorized signatories are legitimate representatives of the SOE.
- ▶ Not allow third parties to accept payments on behalf of the SOE.

⁵⁷ For instance, Peter Wilkinson, *Adequate Procedures: Guidance to the UK Bribery Act 2010*, Transparency International U.K. (2010); Deloitte, “*Guarding Against Fraud and Corruption: The Audit Committee’s Role.*” *The Wall Street Journal*, 22 August 2013.

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- ▶ Not make payments to banks where there is evidence the bank has weak anti-money laundering controls.
- ▶ keep records, where appropriate, regarding the intended commercial use of the payment e.g., to fund operational costs or for direct transmission to the treasury.
- ▶ check and comply with laws and regulations on currency controls. For example, there are often requirements to transfer dollars to the central bank, which can be used to push back against unusual payment requests.
- ▶ Where payments are made for a specific purpose (to fund the purchase of identified goods and services, or for a training or infrastructure program), verify that the funds are effectively used for such purposes (either in connection with making the payment or, where that is not feasible, through a post-payment audit or due diligence process).

Companies should adopt procedures along these lines and disclose them as part of their publicly available anticorruption policy.

4.3. Establish company principles and procedures for responding to misappropriation concerns, and suspend or end operations if misappropriation risks societal harm.

Companies that work with SOEs often accept certain corruption risks, including of misappropriation. Some companies in long-term partnerships with SOEs can feel trapped when there is a deterioration in governance standards and a major corruption scandal breaks. However, there are options and it is better to prepare a possible response in advance than develop a course of action, or inaction, after the event.

Setting out triggers and guidelines on when and how to respond is challenging. The imperative to act is clearer when the risk concerns the company's own transactions. However, when the risk is more indirect—for example, when the misappropriated funds are fungible—companies should not turn a blind eye, especially where remediation is absent and there is clear evidence of societal harm.

A company's senior leadership should convene specific group discussions on how to respond when serious risks arise or when misappropriation is uncovered. This might result in a plan being put in place with escalating responses depending on the severity of the issues. Its steps should be adapted to the circumstances, but could include:

- ▶ raise concerns directly with SOE management
- ▶ engage with other potential allies and oversight actors on a coordinated response
- ▶ share information with relevant law enforcement and regulatory authorities

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- ▶ raise public concerns about the issues
- ▶ suspend specific projects or transactions
- ▶ suspend operations and payments fully
- ▶ move to exit responsibly

To avoid playing an enabling role, companies need to show greater willingness to pursue these options when misappropriation from the SOE is causing societal harms. Coordinating with other companies and stakeholders will increase the impact of such measures.

4.4. Publish payment data on a real-time basis in high-risk deals and jurisdictions.

Payment transparency is a pragmatic and well-established tool for discouraging misappropriation. Hundreds of oil and mining companies have filed “payments to governments” reports thanks to mandatory reporting regulations in Canada, the European Union, the U.K. and other markets, and hundreds more have reported payments via the Extractive Industries Transparency Initiative (EITI). Recently, several commodity traders have also begun disclosing selected payments to SOEs.

However, payment disclosures are less likely to deter misappropriation and facilitate oversight if the data becomes available long after the funds have disappeared. Companies should disclose their payments in as close to real time as possible, especially if the company’s due diligence raises concerns about misappropriation risks. To implement this measure, companies could pursue reporting on a quarterly or rolling basis, and adopt and follow a publicly disclosed materiality threshold.

While adopting a faster timeline, this reporting should otherwise aim to align with existing standards around payment disclosure, specifically:

- ▶ Companies engaged in exploration and production should publish project-level payment data in line with EU and EITI standards.
- ▶ Traders that work with governments and SOEs should report payment data on a sale-by-sale basis, as encouraged in the *EITI Guidelines for Companies Buying Oil, Gas and Minerals from Governments*.
- ▶ Lenders to SOEs, including traders issuing prepayments, should disclose loan agreements on signature, particularly the repayment terms, the amount of fees and interest to be paid, the disbursement of funds, and regular updates on the loan’s repayment by the SOE.

Companies should also publish the related contracts, which provide context important to understanding payment data. At least 20 leading extractive companies, as well as the International Council on Mining and Metals, committed to contract transparency, and it is included in the EITI Standard and the Global Reporting Initiative Standard for the oil and gas sector.⁵⁸

58 Robert Pitman, “*Contract Transparency is an Extractive Industries Success Story—But It’s Not Over Yet.*” NRG, 8 December

4.5. For certain bespoke arrangements, such as resource-backed loans or social investments, push for payment structures that prioritize transparency, oversight and development spending.

Certain scenarios afford companies opportunities to secure additional rights and help safeguard or monitor how funds will be used. These include social investment projects, joint ventures (see Section 5), capacity-building work, and loans or prepayment agreements structured so that funds go toward a pre-identified purpose, such as an infrastructure project. They also include situations of exceptional country risk, such as ongoing conflict, where companies have worked with the authorities or third parties to create special structures.

Overall, the record of bespoke arrangements in such circumstances is uneven, as trying to solve political problems with institutional solutions is difficult.⁵⁹ If such a scenario arises, companies should focus on integrity and oversight, including via:

- ▶ transparency, prioritizing timely information on the use of funds, financial flows, any associated procurement and results achieved
- ▶ financial and legal structures which emphasize accountability, such as escrow accounts for tracking expenditure, staggered payments in line with results, and the proactive use of project audit rights
- ▶ control and oversight of supplier selection, including obtaining veto rights over suppliers
- ▶ payments brought onto the national budget, rather than made through parallel budgets
- ▶ inclusive monitoring systems that involve parliament, civil society and other key oversight actors
- ▶ spending on development priorities, such as those set out in national development plans
- ▶ collective action, if other industry players face a similar scenario.

4.6. Support financial accountability by engaging government, SOE and external stakeholders.

Companies can serve as effective allies of wider efforts to encourage financial accountability and discourage corruption. The aim of such efforts will vary from country to country, and could target improved public and SOE financial management, the reduction of illicit or unaccountable

2020; International Council on Mining and Metals (ICMM), "[ICMM makes new commitment on contract transparency and publishes members' 2020 tax contribution](#)," December 2021; Global Reporting Initiative, GRI 11: Oil and Gas Sector 2021 (2021); EITI, [2019 EITI Standard \(2019\)](#).

59 An example is a World Bank-backed agreement with the Government of Chad for financing an oil pipeline, signed in 2000. The agreement created new structures for channeling oil revenues toward development priorities under enhanced oversight—systems that the government abandoned once oil production increased. Scott Pegg, "Chronicle of a Death Foretold: The Collapse of the Chad-Cameroon Pipeline Project." *African Affairs*, 108/431, 311-320, January 2009.

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forms of spending, greater transparency, or free and effective financial oversight by the public, parliament and government bodies. Companies need not set the agenda, but they should actively maintain an awareness of existing needs and opportunities for reform, so they can help incentivize and support these efforts.

Leveraging their relationships and influence, companies can share their support for financial accountability reforms or express concern about problematic practices with an SOE's senior management or other top government officials. Several companies have described using direct channels in this manner, frequently framing accountability reforms in terms of shared commercial and operational priorities. Along with supporting reform and raising concerns, some companies have provided expertise in relevant areas of compliance.

Engaging with external stakeholders is an essential complement to direct communications. Companies should create and maintain open lines of communication with actors who share concerns around misappropriation and other corruption risks. Some companies have done this in very high-risk markets, demonstrating it is possible, even if not always comfortable. Potential allies include:

- ▶ government actors, including the SOE's government shareholders, relevant parliamentary committees, oversight bodies such as supreme audit institutions, and finance authorities
- ▶ financial institutions that hold SOE accounts, finance transactions or lend to the SOE
- ▶ international organizations, foreign embassies and international financial institutions such as the International Monetary Fund (IMF), which has increasingly acknowledged SOE governance in its publications, Article IV reports and anticorruption conditionality⁶⁰
- ▶ civil society and the media
- ▶ the EITI—a valuable venue for engaging with these players, though it should not be the only strategy used.

In their engagement with SOEs and external stakeholders, companies could pursue the following agendas:

- ▶ Share information and coordinate responses around specific misappropriation concerns.
- ▶ Learn about and contribute to financial accountability reforms.
- ▶ Fill information gaps about the industry and its operations, financial flows and anticorruption practices. In several countries, company engagement has helped build capacity among local civil society groups to engage effectively on sector governance matters.
- ▶ Support open civic space. In certain countries, companies have responded publicly and

⁶⁰ For instance, in Congo-Brazzaville, the Democratic Republic of Congo and Equatorial Guinea, the IMF has pushed for SOE audits—a message that companies could pick up.

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privately to issues of civil society repression.⁶¹ Their actions have included statements and letters to government representatives, collective engagement through industry associations, and working with embassies to leverage the influence of their home governments.⁶²

- ▶ Pursue opportunities for collective action. In some cases, an external party has coordinated a coalition of entities—companies included—to back certain anticorruption reforms.

61 Annabel Lee Hogg and Robin Hodess, *The Business Case for Protecting Civil Rights*, The B-Team (2018); Bennett Freeman, Sif Thorgeirsson and Adele Barzelay, *Shared Space Under Pressure: Business Support for Civic Freedoms and Human Rights Defenders*, Business and Human Rights Resource Centre and International Service for Human Rights (2018).

62 Freeman, Thorgeirsson and Barzelay, *Shared Space Under Pressure* (2018).

5. Protecting joint ventures from corruption

The challenge

When managing corruption risks within a joint venture (JV), the key challenge is that, by definition, the effort requires agreement between two or more parties. One party cannot simply impose its standards on the others. Problems often arise because the different parties have unequal levels of power and influence, or mismatched attitudes, interests and compliance standards. Such scenarios can create commercial, legal and reputational risks for the companies within the venture, and, if corruption ensues, much wider societal harms.

In JVs involving SOEs, the parties often hold different perspectives on key issues. From the perspective of SOEs, particularly those with limited international experience, certain anticorruption procedures can seem burdensome, and in some cases may be inconsistent with government regulations designed to combat the same risks. International companies may view government procedures as roadblocks to achieving the JV's commercial objectives, and as increasing the risk of corruption.

Further issues may arise from the unequal position of the parties to a JV. International companies bringing financing, technology and project management expertise to the venture may have staff who are more highly compensated than their local counterparts, and may rely on head office personnel or systems that are difficult for their local partners to monitor. Similarly, state-owned partners might take issue with an international company's insistence on using

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its global preferred supplier arrangements while blocking the SOE from requiring contracts to be awarded to certain local suppliers that it favors. In addition, operators have different responsibilities than non-operators, and non-operators will face limitations to their ability to influence the integrity agenda. Due to these different roles, the balance of power within JV relationships can vary significantly. This determines the strategies particular companies can pursue for managing corruption risks.

It is often easier to introduce robust anti-corruption features when forming a new JV than to incorporate them in long-standing ventures. In a longstanding JV, if one partner resists adopting or revising anti-corruption procedures, the other is left in a difficult position. It must either go forward without protections in place, risk worsening tensions with its partner, or withdraw from a partnership that could have significant value. Adding to the complexity, establishing anticorruption procedures is only one of many issues on which JV parties need to agree. Companies might feel pressure to prioritize commercial concerns in their negotiations, rather than pushing hard for certain anti-corruption procedures. In addition, the contractual mechanisms and policies agreed only help if they are implemented effectively in the JV's day-to-day operations.

Past cases suggest that several types of corruption risk can arise within the negotiation and operation of JVs—particularly, but not exclusively, in JV procurement. Interviews and the review of court documents indicate the following challenges have arisen in the past:

- ▶ A company has had a JV with an SOE dating back to the 1970s, and has struggled to update the entity's anti-corruption practices. Its efforts to advance this agenda were met with resistance and delay.
- ▶ An international company in a JV failed to respect local content requirements, insisting on using global service companies with connections to major corruption cases.
- ▶ The JV partners pushed corruption risks down to suppliers who were incentivized to stay quiet when problems arose. Monitoring of supplier compliance was limited.
- ▶ On paper, parties to a JV agreed a compliance framework for selecting local suppliers. In practice, the SOE pressured the operator company to use suppliers with political ties, strengthening the dominance of these actors in the sector.
- ▶ Conflicts of interest arose when an SOE was tasked with securing preferential treatment for the venture in regulatory matters, such as obtaining customs exemptions that might otherwise be difficult to secure.
- ▶ A JV's entry into major supply contracts required SOE or ministerial approval, and contractors used bribes and other illegitimate means to influence those approvals.
- ▶ Companies came under pressure from a partner to fund projects which posed heightened corruption risks, such as payments for charitable and political causes, training programs and

contributions to local infrastructure development which lacked adequate due process and integrity protections.

- ▶ JVs have struggled at operational level to control small bribes and facilitation payments relating to customs and local security arrangements. Government officials and SOE staff have also abused per diem payments.

JV partners must find a path through these types of issues if the venture is to operate with high standards of integrity.

Recommendations

5. JV partners should jointly evaluate the venture's anticorruption systems against the following set of principles, developed with prevalent corruption trends in mind. They could then agree and adopt measures to address any concerns or shortcomings.

Below is an aspirational set of principles that JV partners could use to assess their prospective or current approaches to controlling corruption. These are informed by extensive consultations with extractive sector companies, SOEs and anticorruption experts, as well as the analysis of past corruption cases. They primarily address JVs involving an SOE engaged in oil, gas or mineral production. Most of the principles would also apply to other common contractual arrangements involving SOEs such as production-sharing contracts or risk service contracts. Some service companies and commodity traders have also entered JVs with SOEs, and the guidance could prove relevant for these arrangements too.

These principles can help existing or prospective JV partners convene frank and constructive discussions around how they approach anticorruption. Citing an external resource could help individual parties to a JV, or one of its major service providers, to raise anticorruption concerns in a neutral manner, or to justify proposing additional integrity measures. The assessment could take place at moments when reforms and improvements are possible, such as in the wake of a scandal, when the host country or the SOE has new leadership, or when entering a new phase of operations.

Above all, the principles should stimulate consensus building. JVs are ultimately “relationship contracts,” so achieving shared understanding and ownership among partners is crucial. The

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pursuit of these principles could help manage the differences among partners noted above, and leverage shared interests in prioritizing integrity, avoiding controversy and controlling costs.

Given the wide range of possible anti-corruption practices, these principles focus on what the JV wants to substantively accomplish when it comes to lowering corruption risks. These examples of controls are not comprehensive and are illustrative, rather than promoting any one procedure or provision.

Principle 1. The JV promotes a culture of integrity.

In practice, this might mean:

- ▶ Anticorruption features prominently in leader statements, board discussions, staff inductions and evaluation, and other important forums, creating a consistent “tone from the top.”
- ▶ The JV partners establish a joint committee tasked with designing tailor-made procedures adapted to the specifics of the JV, and with reporting their results to the JV’s senior management and governing structure, such as a board or management committee.
- ▶ The JV partners each nominate anti-corruption compliance leaders to the venture.
- ▶ A code of conduct is adopted and implemented at operational level, along with other policies designed to mitigate corruption risk, including policies on anticorruption, procurement, charitable and political contributions, and travel, gifts and hospitality.
- ▶ The JV adopts appropriate internal financial controls based on a well-recognized international standard.
- ▶ The JV conducts regular training for appropriate staff on the code of conduct and other relevant policies, and implementation of internal financial controls.
- ▶ Appointments and remuneration of JV management and personnel are decided with openness, integrity and a commitment to meritocracy.
- ▶ Staff are encouraged to report red flags or instances of corruption.
- ▶ The JV maintains a whistleblowing mechanism, protecting whistleblowers against retaliation and accused wrongdoers against unfounded anonymous allegations.
- ▶ The JV or its operator convenes a working group or another regularized channel of communication with its major suppliers that discusses corruption risks on an ongoing basis. Engagement up front can reduce the need for audits and investigations later.
- ▶ The JV responds effectively to integrity concerns when they arise, following a set of pre-agreed steps and an escalating series of measures.

Principle 2. The JV deploys anticorruption safeguards based on a sound assessment of risk.

In practice, this might mean:

- ▶ Prospective JV partners assess corruption risks and the societal harms they may cause prior to entering into any new venture. (See Section 1 on SOE due diligence.)
- ▶ When formed, the JV commits to regularly undertaking corruption risk assessments which consider a broad range of corruption typologies in the sector,⁶³ covering both risks to the JV and its parties, and to citizens of the host country. The risks identified during the JV's third-party due diligence (see below) feed into this assessment.
- ▶ Because corruption risks often cluster around procurement, major suppliers join the assessment process to encourage open communication and strategizing around risk mitigation, and to create shared incentives among all parties to voice corruption concerns and avoid risks.
- ▶ Senior leadership at the JV partners meet to consider the results of the risk assessment and agree mitigating actions.
- ▶ There is regular follow-up and re-evaluation of risks.
- ▶ Operational or work plans submitted by the JV operator and approved by the partners contain a dedicated field on corruption risks.

Principle 3. The JV manages procurement with integrity and does not enable corrupt practices.

In practice, this might mean:

- ▶ The parties (either in the JV agreement or through governance bodies) determine at the outset who will be responsible for contracting and what approvals are required. The JV works to a written procurement policy.
- ▶ The JV selects third parties through an open and competitive process as often as possible, and requires heightened sign offs for single-source awards.
- ▶ The JV prioritizes transparency in its procurement, including public reporting on procurement processes, supplier identities and spending on suppliers.⁶⁴

63 For typologies of extractive sector corruption, see Alexandra Gillies, Matthieu Salomon, Sebastian Sahla and Tom Shipley, *Diagnosing Corruption in the Extractive Sector: A Tool for Research and Action*, NRG (2021); OECD, *Corruption in the Extractive Value Chain. Typology of Risks, Mitigation Measures and Incentives* (2016).

64 For more discussion on supplier oversight and transparency, see Robert Pitman and Kaisa Toroskainen, *Beneath the Surface: The Case for Oversight of Extractive Industry Suppliers*, NRG (2020).

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- ▶ Tenders are open only to contractors on pre-qualification lists or specific qualification lists established and maintained through appropriate due diligence procedures.
- ▶ Bidders identify corruption risks and mitigating strategies in a designated section of tender documentation.
- ▶ The procurement policy explains any specific procedures for promoting the use of local contractors and international contractors that commit to local employment, including parameters and guidelines designed to ensure integrity.
- ▶ The JV partners commit to not working with contractors or agents which exhibit certain red flags. (See Recommendation 3.2.)
- ▶ The JV evaluates engagements with politically exposed third parties for the societal harms they might cause and their potential for enabling corruption, and avoids engagements with such potential. (See Recommendation 3.5.)
- ▶ The JV has and follows an agreed approach, including heightened approvals, for contracting with affiliated parties (e.g., international company or SOE affiliates, or preselected service companies).
- ▶ Contracts awarded by the JV systematically contain clauses providing for termination by the JV in case of a violation of business ethics standards, either with no compensation or at least with reduced compensation designed to eliminate profit elements.
- ▶ The JV cascades strong integrity standards and due diligence obligations to its subcontractors and suppliers. It examines and records supplier compliance systems as an explicit component of its due diligence.
- ▶ The JV engages its suppliers as key partners in preventing corruption and guards against pushing corruption risks down the supply chain, by measures such as regularly convening suppliers to discuss corruption concerns, encouraging them to raise such concerns and regularly conducting joint risk assessments.
- ▶ The JV does not require or allow the use of agents in its procurement, and to the greatest extent possible does not use agents in its host government relations. Any remaining agents are subject to special controls. (See Section 2.)
- ▶ The JV monitors major suppliers' anticorruption procedures and asks for information on their effectiveness.
- ▶ The JV avoids favoritism by applying effective and consistent responses to non-performance, cost overruns and other performance shortfalls by contractors.

Principle 4. The JV safeguards financial flows against corruption.

In practice, this might mean:

- ▶ The JV partners include misappropriation risks as part of their corruption risk assessment and partner due diligence. (See Recommendation 4.1.)
- ▶ As part of its internal financial controls, the JV puts in place enhanced standard procedures to minimize risks, such as “several pairs of eyes” to approve payments, and restrictions on cash payments. Recommendation 4.2 lists additional financial controls that companies should apply to payments to SOE and government accounts.
- ▶ There is a simple and transparent structure for financial flows from and to JV partners, and to designated government agencies.
- ▶ The JV establishes an audit committee with the authority to review all transactions and question senior personnel involved in the venture.
- ▶ There is increased scrutiny, including by the audit committee, of transactions which are at higher risk of corruption, such as charitable and social investment contributions.

Principle 5. The JV guards against potential conflicts of interest and inappropriate forms of political influence.

In practice, this might mean:

- ▶ If the SOE plays a regulatory role in addition to its commercial role as a JV partner, the JV establishes procedures to manage potential conflicts of interest. For instance, some JV operators designate separate personnel to engage with the SOE’s regulatory functions.
- ▶ Key decisions are debated and made through formal channels and committees, reducing the risk of *ad hoc* political interference in the JV’s operational decisions.
- ▶ The code of conduct applied in the JV includes provisions around lobbying and engagement with government decision-makers.
- ▶ The JV requires written documentation of its interactions with government officials, including gifts and hospitality.

Principle 6. The JV operates to global transparency standards and proactively engages with other stakeholders on building integrity in the sector.

In practice, this might mean:

- ▶ Transparency is used as a risk-reduction approach and not a box-ticking exercise.

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- ▶ The JV reports project-level payment data in line with EU and EITI standards. The JV's contracts with the government are fully disclosed and it prioritizes transparency in its procurement processes.
- ▶ The JV proactively discloses relevant information for managing corruption risk, such as anticorruption policies and procedures, conflicts of interest policies, and approaches to managing political exposure.
- ▶ The JV partners publicly report their beneficial owners. The JV works toward requiring beneficial ownership disclosure from its large and high-risk suppliers. (See Recommendation 3.4.)
- ▶ The JV partners engage stakeholders on integrity matters, and initiate or participate in collective action initiatives that seek to build integrity in the sector. (See Recommendation 4.6.) Such stakeholders might include government agencies, parliament, civil society, international financial institutions and foreign embassies.

Strategies for achieving and sustaining the principles

Given the challenges outlined above, many existing JVs will achieve these principles over time, rather than overnight. International companies tend to focus on the contract as the means to achieve standards. This is important, but not in itself sufficient. Below are three pathways for exercising influence and supporting integrity within the JV.

Governance structures

Companies seeking to adopt these principles can negotiate for influence in the JV's governance structures and use this influence to promote appropriate policies. Options include:

- ▶ requiring management and audit committee representation, including for non-operators—a priority for monitoring the control environment and especially risks related to procurement
- ▶ ensuring JV partners employ a recognized external auditor, to bring greater scrutiny and help control against corruption
- ▶ appointing dedicated JV compliance officers
- ▶ establishing representation and secondees in key functions, and rotation of roles and responsibilities, including embedding employees in the procurement system
- ▶ ensuring that non-operator company representatives on JV committees have compliance among their priorities, and look out for and act on red flags for corruption
- ▶ requiring frequent and thorough compliance reporting from the JV management

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Contracts

The JV contract underpins the relationship and sets the tone for how the partnership will run. Representatives from several companies indicated that their newer JV contracts contain updated integrity and risk-mitigation provisions which could serve as instructive models.

Useful contractual features could include:

- ▶ veto rights for companies on certain types of expenditure (e.g., donations, charitable and social contributions)
- ▶ obligatory compliance with set procurement procedures
- ▶ strong criteria and limitations on single-source procurement
- ▶ audit rights (which must be used proactively and not simply when concerns are raised)
- ▶ mandatory compliance reviews when concerns are raised
- ▶ notification, indemnification and termination rights
- ▶ restrictions and veto rights on transfers of ownership

While contractual measures can help advance many of the recommendations made in this document, some companies warned against over-reliance on contractual fixes. They noted that the anticorruption controls implemented during the JV's operations are what will truly drive positive change. For instance, when contractual violations or issues arise, many companies will not want to pursue costly disputes with their powerful SOE partner or walk away from sizeable investments.

Exchange of good practices

Some companies reported positive experiences with training and sharing good practices with SOE or other JV partners to develop their compliance cultures and capabilities. It may also be valuable to engage key external actors in these initiatives, including large subcontractors who often best understand how well corruption risks are being managed on the ground. The exchange of personnel is another useful tool. For instance, through the Compliance Without Borders program managed by the Basel Institute on Governance, and the OECD's Trust in Business initiative, compliance experts are seconded to SOEs to share skills and develop compliance capacity in areas such as procurement and contracting processes, third-party management and conflicts of interest.⁶⁵

Operationally, the exchange of good practices will take place most concretely through a collaborative approach to compliance management. For example, jointly commissioning and reviewing risk assessments is a way of putting important issues on the table, even if there may be sensitivities in discussing the problems.

⁶⁵ OECD and Basel Institute on Governance, *Compliance Without Borders* (2018).

Anticorruption recommendations for state-owned enterprises

State-owned enterprises (SOEs) in the oil, gas or mining sectors should consider adopting the measures recommended below as part of their efforts to prevent corruption.

Oil, gas and mining SOEs are highly diverse. Some have extensive anticorruption systems and are subject to actively enforced antibribery and other anticorruption laws. The guidance offers these SOEs ways to shore up well-established processes in light of prevailing corruption trends and evolving good practices. Many smaller SOEs and those that engage in fewer commercial operations have more limited anticorruption policies, capacities and resources. For lower-capacity and smaller SOEs, the guidance offers possible starting points on their journey toward developing stronger integrity systems. They may prefer to choose a few priorities from among the recommendations where they could focus their efforts during an initial phase.

Achieving progress on these fronts will help SOEs of all sizes to inspire investor confidence, attract partners and suppliers committed to integrity, improve operational efficiency, reduce costs, avoid controversy, and protect their countries from the harms that corruption can inflict.

The five recommendations below complement the accompanying guidance for private-sector companies that work with SOEs, and align with the five sections of this guidance. Action by both private-sector and state-owned companies is essential to reducing corruption risks.

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The recommendations:

- ▶ reflect extensive consultations with extractive-sector stakeholders
 - ▶ target specific corruption vulnerabilities apparent in the extractive sector, based on analysis of dozens of past corruption cases involving SOEs (rather than offering a comprehensive approach to corruption risk management)
 - ▶ include concrete measures primarily intended for SOE management to adopt, whereas some other sources of guidance target the SOE's government owners
 - ▶ draw from recent SOE reforms, other industry good practices, as well as several sources of guidance which represent valuable and complementary resources
- focus on the roles played by SOEs within their home countries. When a SOE operates overseas, the other sections of this guidance would apply.

NRGI anticipates engaging with SOEs as they work to improve their integrity systems, and welcomes feedback and exchange on the recommendations that follow.

Recommendations

Note: For the purposes of this guidance, private-sector companies that partner with SOEs are referred to as “companies” and state-owned enterprises, while also companies, are referred to as “SOEs.”

SI. Adopt and publicly announce governance practices that demonstrate the SOE's commitment to operating with integrity.

Adopting these foundational measures will help an SOE prevent corruption, while also signaling to investors, partners, suppliers, employees and the public its commitment to integrity. The OECD, the World Bank and compliance guidance for privately owned companies all provide more detailed coverage of these topics.

SI.1. Corporate governance

A strong, clearly defined framework for corporate governance can help insulate the SOE and its operations from political and personal agendas. This begins with an independent, professional and empowered board. In particular, stakeholders emphasized the value of an active board audit committee, separate roles for board chair and CEO, and board appointment of the CEO. The SOE's shareholders should be identified and their roles and responsibilities clearly established. Board and senior staff appointments should follow well-defined meritocratic processes that emphasize

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technical expertise rather than political connections. The SOE should be subject to regular, independent external audits and publish the results. When the SOE plays both regulatory and commercial roles, it should indicate clearly how it avoids potential conflicts between them.

SI.2. Anticorruption policies and practices

The SOE should establish codes of conduct or similar policies that address topics including third-party due diligence and the procurement of goods and services (see Recommendation S3), board and senior management remuneration, conflicts of interest (see Recommendation S3), nepotism, bribery, facilitation payments, gifts and hospitality, political contributions, charitable donations and sponsorships, solicitation and extortion. The SOE should also create an anonymous channel for reporting suspicions or concerns, such as a whistleblower hotline, and protect anyone raising concerns from recrimination. The SOE should look to partner with firms that share a commitment to working to high integrity standards. The SOE's third parties should be contractually required to follow its anticorruption policies and it should monitor their compliance with these policies.

The SOE should have a dedicated compliance function with professional staff, which operates with independence and visible leadership support, and has direct access to the board. To protect independence, it is important to separate this function from commercial and procurement units. An empowered and qualified internal audit unit is also important.

The SOE should regularly review the effectiveness of its anticorruption measures through a process that involves the board.

There is no replacement for an organizational culture that prioritizes ethics and integrity, premised on a strong tone from the top. All senior management, relevant personnel and high-risk suppliers should regularly receive training on anticorruption policies and practices.

SI.3. Transparency

The Extractive Industries Transparency Initiative (EITI) Standard is a good reference for SOE transparency. Its requirements include disclosure of the SOE's contracts, payments, financial transfers to and from the government, commodity sales, resource-backed loans and quasi-fiscal expenditures.

The SOE should also publish annual reports and audited financial statements.

To help prevent corruption, the SOE should also disclose detailed anticorruption policies, including the code of ethics that applies to employees and third parties. It should also prioritize transparency in high-risk processes which have proven vulnerable to corruption across many countries, including procurement, local content, commodity trading and social programs. For

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instance, for commodity trading, the SOE should disclose the rules and contracts that govern commodity sales; information about tenders, including lists of prequalified and selected companies, and the buyer, volume, price and date of individual sales.

In addition, the SOE should report their beneficial owners, including the legal name of the state body, agency or office that holds the interest.

It should also identify its subsidiaries and joint ventures, and work toward disclosing the names and beneficial owners of the entities that hold shares in these entities.

SI.4. Engagement and oversight

An SOE should invite and support active oversight and stakeholder engagement, including with its government shareholders, the legislature, oversight institutions such as anticorruption commissions and supreme audit institutions, the media, civil society groups and the public. To advance this, the SOE should participate actively in the country's EITI process, where applicable, or hold regular meetings with the relevant stakeholders. As the OECD notes, SOE representatives should “refrain from actions that serve to repress or otherwise restrict the civil liberties, including liberties to criticise or investigate, of civil society organisations, trade unions, private sector representatives, the public and media.”

SI.5. Investigations and penalties for corrupt behavior

When credible allegations of corruption arise, the SOE and its government should investigate, apply dissuasive penalties as warranted, and engage in remediation and reform.

OECD guidance on enforcement and penalties

Corruption must be met with appropriate sanctions. The OECD's 2019 *Guidelines on Anti-Corruption and Integrity in SOEs* offers valuable instruction on this matter:

“Civil, administrative or criminal penalties for corruption or other unlawful acts should be effective, proportionate and dissuasive. They should be applicable to both natural and legal persons, including SOEs....”

Transparent procedures should be developed to ensure that all detected irregularities in and concerning SOEs are investigated and prosecuted when necessary, in accordance with domestic legal procedures. Enforcement of provisions in the legal framework should be rigorous and systematic, and ensure that SOEs are not given unfair advantage or protected by their ownership. Furthermore:

- i. Supervisory, regulatory and enforcement authorities should have the authority, integrity and resources to fulfill their duties in a professional and objective manner while guaranteeing due processes and respecting fundamental rights. Moreover, their rulings should be without undue delay and, as appropriate, transparent and fully explained.
- ii. Investigation and prosecution of cases of corruption or related unlawful acts involving SOEs should not be influenced by considerations of national economic interest, the potential effect upon relations with another State or the identity of the natural or legal persons involved.
- iii. Relevant state bodies should co-operate fully with investigations involving SOEs or the state as enterprise owner, and they should encourage SOEs to do likewise.

When corruption or irregular practice has been detected, the ownership entity should have processes for follow-up with SOEs to support the mitigation of recurrence. This could include, inter alia, encouraging the SOE to develop an action plan based on a root-cause analysis, and to communicate lessons learned throughout the SOE hierarchy. The state should consequently assess need for reforms within SOEs or in the exercise of its duties.”

Source: OECD, Guidelines on Anti-Corruption and Integrity in SOEs (2019), 31.

In the extractive sector, numerous foreign bribery cases and other legal proceedings have revealed credible allegations that SOE officials engaged in corruption, but many of those officials subsequently faced no serious investigation or penalties in their home country. To deter corruption, an SOE and its government owners have a responsibility to act when suspicions of corruption arise, even if this implicates their own officials or politically powerful parties.

The SOE should establish procedures for handling situations when allegations arise, follow them rigorously, and cooperate with investigations by other legal authorities. Law enforcement in the SOE’s country also has a major role to play. See the box above for more on this topic from the OECD.

S2. Reduce the use of high-risk agents by companies seeking business from the SOE.

Agents have featured in many corruption cases involving SOEs, particularly when companies use them to help secure new business from an SOE. (See Section 2.) To reduce the number of these high-risk actors, the SOE should reduce the need for private sector companies to use agents, particularly in its procurement processes and commodity-trading business. For any remaining agents, the SOE should adopt additional controls.

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While definitions vary, the term “agent” typically refers to third-party individuals or organizations that represent a company or act on its behalf.

S2.1. Map and monitor the use of agents.

Mapping the use of agents by companies seeking business from an SOE will allow the SOE to understand the current state of play and generate a baseline for efforts to reduce agent use. Tracking the use of agents also enables the SOE to spot worrying practices, such as companies using business development agents that lack experience and qualifications, or multiple companies using the same agent in ways that appear unusual. To inform the mapping, the SOE could require suppliers, traders or other relevant entities to report whether they use agents and, if so, the identities of those agents. For instance, Petrobras requires prospective suppliers to provide this information before they can participate in a tender. Any mapping effort should review whether other entities, such as local equity partners or consultants, are performing agent-like functions, as this can present equal corruption risks. Section 2.1 provides guidance on categorizing agent functions.

S2.2. Consider banning applicants from using representative business development agents.

Corruption risks run high whenever awards or tenders involve many intermediaries seeking to influence SOE officials. The SOE could choose to prohibit traders, suppliers or other third-party applicants from using agents in certain circumstances. Such a ban would need a specified scope and clear definitions. For instance, the SOE could ban companies from using agents to represent them when seeking new business from the SOE, or when securing certain contract extensions, renewals or regulatory approvals. Such a ban could also apply to agents that perform wider representative

Sample agent prohibition

The Abu Dhabi National Oil Company includes in its 2021 *General Terms and Conditions for the Sale of Crude Oil*, the following provision prohibiting the use of agents:

“19.3 Buyer represents that:

- (a) this Contract is entered into without the assistance or intervention, direct or indirect, of any broker, intermediary, commission agent or any similar person, firm or corporation (each hereinafter referred to as an “Agent”);
- (b) neither Buyer nor any of its Affiliates, directors, officers, employees, agents, representatives

and consultants have engaged the services of any such Agent for the purposes of exercising or obtaining improper influence in connection with this Contract; and

- (c) no Contractors fee or other compensation has been paid or is payable by Buyer or any of its Affiliates, directors, officers, employees, agents, representatives and consultants to any Agent in connection with this Contract.”

functions, such as sourcing new business opportunities, making introductions, negotiating or acquiring information on the company’s behalf, or other activities requiring interaction with officials.

Several national oil companies have taken steps in these directions, as illustrated in Box 2. Such measures will only be practical if the SOE takes steps to create an even playing field that is open and accessible to new entrants, such as by providing clear and comprehensive information about the tender process to prospective participants.

S2.3. Reduce the practical need for agents.

In some cases, companies use agents when procurement systems are confusing, unpredictable or out of date, or when award decisions are discretionary and require earning favor from individual SOE officials or other influential figures. Adopting transparent, standardized and digitized processes and the use of open tenders in areas such as procurement and applications for approvals will reduce the need for local agents, and the risk of bribes and facilitation payments. Companies will be able to compete for opportunities and secure the necessary approvals without hiring an insider to help them navigate the system. For instance, companies should not have to hire an agent to hand-deliver physical copies of tender documents to an SOE.

Elsewhere, companies often hire agents as a way of meeting the SOE’s local content requirements. The SOE could evaluate whether these agents are effectively delivering on the aims of the local content program, such as growing local business capacity, or whether the use of agents is only benefiting a few well-connected individuals, creating corruption risks and adding to industry costs. If the latter, the SOE should take steps to reduce the use of agents.

S2.4. Where agents remain, adopt controls and avoid high-risk practices.

Where companies continue to use agents in their SOE engagements, the SOE can take measures to reduce corruption risks, including:

- ▶ Publishing a policy that details the SOE’s approach to agents.
- ▶ Requiring that when companies register to compete in a tender or other award process, they

name any business agents they use and provide a justification for this use. Collecting this information could be a standard part of the prequalification or application process for third parties. If an SOE assigns levels of risk to third parties as part of its due diligence system, the use of agents can then be considered as a risk factor that informs the overall risk assessment. See the box below for more on how Petrobras implements a similar measure.

- ▶ Performing further scrutiny when companies use agents, including enhanced due diligence on the company and the agents, and examining whether an agent is providing a legitimate service and whether they have any connections to politically exposed persons.
- ▶ Requiring all entities participating in a tender or contract, including agents, to agree to robust anticorruption measures.
- ▶ Creating and publishing a register of agents, accepting only those that have fulfilled integrity and capacity criteria. The register could include the name of the agent and its representatives, its beneficial owners, its clients and the type of service provided.
- ▶ Prohibiting companies from engaging with agents that exhibit a pre-established set of red flags. (See Recommendation S3.4 below.)
- ▶ Discouraging corruption-prone types of fee, such as success fees, by publishing standard fee rates for certain services.
- ▶ Requiring SOE personnel who meet with suppliers about new business opportunities (e.g., a future or ongoing tender) to attend with more than one person and submit written minutes of the meeting.
- ▶ Securing buy-in from SOE personnel who interact with agents. Capacity building and culture change are often required within the SOE if agents have played a big part in the system for many years. SOE personnel may have established close and mutually beneficial relationships with agents. Staff training and consultation can help.

S3. Avoid conflicts of interest and the inappropriate participation of politically exposed persons among the SOE's third parties.

Across many countries, SOEs have allocated contracts or licenses to entities connected to a politically exposed person (PEP). In some instances, the entity received this opportunity due to its industry credentials, and the PEP's involvement did not create a conflict of interest. But in others, the PEP's involvement caused the SOE to treat the entity favorably, or the contract became a vehicle for siphoning public funds into private pockets.

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The following measures can help avoid these scenarios. They should apply to a wide set of SOE processes, including the award of exploration or production licenses and equity shares in producing assets, procurement, commodity trading deals, asset sales and acquisitions, local content programs and social projects.

S3.1. Adopt, disclose and enforce strong policies on conflicts of interest, “revolving door” concerns and asset declarations.

In a publicly available policy, the SOE or its state owners should define clear rules and procedures for managing conflicts of interest. The policies should include prohibitions against senior SOE officials holding commercial interests in the sector, and against SOE personnel participating in decisions regarding related parties (e.g., entities tied to their family or associates). Policies should also cover SOE officials accepting gifts, hospitality and other favors from third parties that could impact their incentive to act in the best interest of the SOE's shareholders. Even apparent or potential conflicts of interest can damage public trust in an institution.

The SOE should also establish restrictions on personnel moving between the SOE and the private sector, including requiring SOE officials to undertake a “cooling-off period” before joining or acquiring interests in a company active in the sector. Appointments from the private sector should receive enhanced vetting and be subject to conflict of interest controls.

As an essential complement to these measures, the SOE should establish and implement a robust asset disclosure policy for its senior personnel and board members. These policies should be actively enforced with serious, dissuasive penalties for violations.

Because SOE personnel are not the only concern, it is equally important that other senior public officials, such as those in the presidency, sector regulators and sector ministries, are also subject to strong conflict of interest, revolving door and asset declaration procedures.

S3.2. Implement open, competitive, rule-bound and transparent award processes that visibly prioritize integrity.

The SOE should seek to allocate business opportunities through processes that are open, competitive, rule-bound and transparent. Such a system will limit discretion and opportunities for political influence, make bribery less enticing, and elevate financial and commercial selection criteria over political or personal ones. In particular, the SOE should avoid single-source awards as much as possible and use them only following enhanced approval procedures. As above, e-procurement systems and other digitization measures often help. To enhance transparency and oversight, the SOE should disclose full information concerning the bidding, awarding and delivery phases. The Open Contracting Principles provide useful guidance.

The SOE should also clearly and publicly define its integrity standards, which helps

The Petrobras approach to supplier “integrity due diligence”

In the wake of the “Car Wash” corruption scandal, which centered on SOE procurement, Brazil’s national oil company Petrobras undertook widespread anticorruption reform. Along with increasing its use of competitive tenders and digitizing additional elements of its procurement processes, one key reform concerns how Petrobras vets its suppliers.

Entities that seek supply contracts from Petrobras must first complete an integrity due diligence questionnaire. The form includes questions about the entity’s

- ▶ key personnel and beneficial owners
- ▶ connections to government entities and public officials
- ▶ corruption record, including any investigations
- ▶ ethics and compliance programs
- ▶ use of agents or intermediaries to obtain new business, generally and with respect to Petrobras, and the identity of any such agents.

Using this questionnaire, the Petrobras compliance team assigns each entity a high, medium or low integrity risk score. Since 2015, it has scored over 30,000 entities.

For entities that receive a medium score, the team examines the information and additional controls are put in place. Those that receive a high score are not eligible to seek contracts from Petrobras (with a narrow set of exceptions). Many entities that scored poorly over the years have taken measures to improve their performance. The Petrobras team cites this record as evidence that the integrity system is strengthening local suppliers, rather than harming them. During the first half of 2021, only around 2 percent of applicants received high scores.

Sources: Petrobras, “Integrity Due Diligence Questionnaire” (2021); Petrobras, “How a bidding procedure works” (accessed 2021); Petrobras, “Integrity Due Diligence (IDD),” presentation, August 2021.

communicate its expectations to prospective third parties. For instance, the SOE should require all third parties to follow its anti-corruption policies or equivalent standards, and make these standards available publicly and at the start of any award process.

S3.3. Require applicant third parties to report their beneficial owners and other anticorruption information, and use this information to avoid high-risk entities.

Through a prequalification or application process, the SOE should require all prospective third parties to report:

- ▶ their directors, top personnel and beneficial owners
- ▶ any personnel or beneficial owners who are PEPs, based on a strong PEP definition
- ▶ whether they use agents (see S2.4 above)
- ▶ information about their anticorruption and compliance programs
- ▶ past investigations or convictions for corruption

The SOE's staff should review this information, verify it for high-risk third parties and identify red flags that indicate a potential corruption risk. When red flags arise, the transaction should be elevated for review by the SOE's compliance division and senior management. In some cases, the SOE may move forward and adopt enhanced anticorruption controls to mitigate risks. In others, it should refuse to work with the entity.

In the wake of the “Car Wash” corruption scandal, the Brazilian government and the national oil company Petrobras implemented wide-ranging anticorruption reforms. The box above describes how Petrobras screens suppliers for corruption risks.

S3.4. Prohibit working with certain types of high-risk entity.

The SOE should prohibit engagement with certain limited categories of entity, and publish these prohibitions in its anticorruption policy. These categories should include:

- ▶ entities that will not report their beneficial owners
- ▶ entities whose key personnel or beneficial owners include:
 - ▶ an SOE or government official with a conflict of interest relating to the business the company is seeking⁶⁶
 - ▶ a former official who recently left such a position of influence, for example, within the last 24 months⁶⁷

66 The OECD defines a conflict of interest as “a conflict between the public duty and private interests of a public official, in which the public official has private-capacity interests which could improperly influence the performance of their official duties and responsibilities.” Conflicts in this context can take many forms, most seriously when an official holds decision-making power or has access to inside information concerning the business a company is seeking. OECD, “*Recommendation of the Council on OECD Guidelines for Managing Conflict of Interest in the Public Service*,” OECD/LEGAL/0316. 28 May 2003.

67 This recommendation does not mean conflicts of interest end after this period. As the Financial Action Task Force (FATF) notes, “The handling of a client who is no longer entrusted with a prominent public function should be based on an assessment of risk and not on prescribed time limits.” FATF, *FATF Guidance: Politically Exposed Persons (Recommendations 12 and 22)* (2013).

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- ▶ individuals in violation of the SOE or producer country's prohibitions on public officials acquiring commercial interests⁶⁸
- ▶ individuals or entities convicted or otherwise credibly shown to have engaged in corruption-related offenses, and where evidence of adequate remediation is not found.

S3.5. Work to disclose a register of third parties that includes beneficial ownership information.

Beneficial ownership transparency is spreading rapidly, and SOEs can support this essential anticorruption practice within the extractive sector. The SOE should publish a register of the third parties with which it contracts that includes beneficial ownership information. To move toward this goal, the SOE could take a phased approach and begin by reporting beneficial ownership information for its joint venture (JV) partners, large suppliers and high-risk suppliers.

S4. Safeguard SOE finances from misappropriation.

SOEs often play an important role in revenue collection, receiving production shares, cash calls, loans and payments for crude oil, among other types of payment. In some instances, SOE or other public officials have misappropriated or misused these funds. NRGi reviewed 21 corruption cases where illegal or illegitimate SOE spending took place in countries in Asia, Africa, Eurasia and Latin America. Some of these diversions were clearly illegal, such as when officials directly rerouted SOE funds into their private accounts. Others involved the allocation of funds for illegitimate purposes, such as spending on inflated contracts for politically connected companies, or patronage-driven spending ahead of elections. While some of these practices were legal under domestic law, they still fit under common definitions of corruption.

The following anticorruption measures should supplement the fundamental practices noted under recommendation A, such as conducting independent audits and having an empowered board audit committee.

S4.1. Prohibit or avoid certain high-risk transactions.

The SOE should avoid certain practices that have arisen in multiple corruption schemes. These practices should be prohibited or require approval from the compliance unit, senior management and board. They include:

- ▶ accepting cash payments
- ▶ accepting payments from agents, rather than the companies they represent

68 NRGi reviewed over 50 mining and oil laws and found that about half contained prohibitions on PEPs holding interests in the sector. Erica Westenberg and Aaron Sayne, *Beneficial Ownership Screening: Practical Measures to Reduce Corruption Risks in Extractives Licensing*, NRGi (2018).

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- ▶ requiring or allowing companies to pay funds owed to the SOE to third parties instead
- ▶ accepting payments that violate applicable laws
- ▶ using banks that exhibit a weak anti-money laundering record or other red flags of corruption
- ▶ making political contributions

The OECD *Guidelines on Anticorruption and Integrity in SOEs* provide more detailed guidance on financial management practices, including on following recognized international accounting standards and engaging with oversight bodies such as supreme audit institutions.⁶⁹

S4.2. Implement thorough and timely payment and contract transparency.

Payment transparency is a pragmatic and well-established tool for discouraging misappropriation.⁷⁰ However, payment disclosures are less likely to deter misappropriation and facilitate oversight if the data becomes available long after the funds have disappeared.

The SOE should disclose the payments it receives in as close to real time as possible. While adopting a faster timeline, this reporting should otherwise aim to align with existing standards, such as the EITI Standard, specifically by publishing:

- ▶ project-level data on payments from exploration and production companies, in line with EU and EITI standards⁷¹
- ▶ the full text of any exploration and production contracts to which the SOE is a party, which provide the contextual information needed to understand payment data
- ▶ sale-by-sale data on commodity sales, as encouraged in the *EITI Guidelines for Companies Buying Oil, Gas and Minerals from Governments*
- ▶ information on loan agreements, including prepayments with traders, that include the loan agreement itself upon signature (particularly the repayment terms, the amount of fees and interest to be paid, and the disbursement of funds) and regular updates on the loan's repayment by the SOE.

S4.3. Guard against cost inflation and commodity price manipulation as common channels for revenue loss.

In many past cases of corruption, SOEs allowed certain politically favored companies to collect

69 OECD, *Guidelines on Anti-Corruption and Integrity in SOEs (2019)*.

70 Hundreds of oil and mining companies have filed “payments to governments” reports, thanks to mandatory reporting regulations in Canada, the EU, the U.K. and other markets. Hundreds more companies and over 50 governments and SOEs have reported payments via the EITI. Recently, several commodity traders and SOEs have also begun to disclose commodity trading payment data.

71 EITI, *The EITI Standard* (2019); EU, “Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings” (2013).

undue earnings. Most often, SOEs paid inflated prices for goods and services, or awarded overly favorable terms to commodity traders. The SOE should adopt cost audits and other measures to actively guard against and detect such practices.

S4.4. Support public financial accountability efforts.

In many resource-rich countries, SOEs receive and manage a major portion of public revenues. As a result, public financial management reforms, particularly around accountability and integrity, will benefit from SOE cooperation. However, in some instances, SOEs have withheld data and obstructed reform. To proactively support reform, the SOE should openly engage with stakeholders, including government agencies such as the finance ministry and supreme audit institution, the EITI and Open Government Partnership processes (if applicable), international financial institutions, the media and civil society.

S5. Working with partners, evaluate joint venture anticorruption systems against a set of principles, and adopt measures to address any shortcomings.

SOEs often rely on their JV partners to prevent corruption, especially when partners are the ones operating oil, gas or mining assets. To ensure JV anticorruption systems are working well, the SOE could convene the partners to conduct a review. Section 5 of this guidance presents an aspirational set of principles that JV partners could use to assess their prospective or current approaches to controlling corruption. These primarily address JVs engaged in oil, gas or mineral production, but most would also apply to production sharing contracts or risk service contracts involving SOEs, or to JVs in other business segments such as trading or construction.

A few practical ideas from Section 5 are particularly relevant for SOEs. The SOE can help its JV partners by drawing clear lines between its commercial and regulatory functions, rather than leaving this potential conflict for them to manage. When an SOE is not the JV's operator, it could require the operator to include in its work plans a dedicated field in which it assesses corruption risks and identifies their risk mitigation approaches. If the SOE seeks to strengthen its compliance function, it could seek support from its larger JV partners as a source of expertise.

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