



# Beneath the Surface: The Case for Oversight of Extractive Industry Suppliers

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## Key messages

- In extractive industry projects, suppliers of goods and services do significant work. These companies range from large multinational conglomerates to small local firms.
- Between 2008 and 2017, oil, gas and mining companies spent, on average, just under a trillion dollars a year on suppliers. Though this figure will shrink in 2020 as a result of the coronavirus pandemic, spending on suppliers will remain one of the major financial flows from extractive industry projects.
- Without effective internal management systems and strong external oversight, weak governance of suppliers can lead to:
  - Cost overruns that undermine company profits and government revenues
  - Suboptimal taxation of supplier profits, resulting in lost tax revenues
  - Local procurement systems that fail to deliver the intended economic benefits to host countries or communities
  - Corruption risks including bribery, favoritism and state capture
- Transparency can help improve supplier oversight. In particular, the private sector, state-owned enterprises and host governments should publicly report on procurement processes, supplier identities, spending on suppliers and supplier taxation.
- A number of global reporting standards and ad hoc disclosure practices set valuable precedents that extractive industry stakeholders can build upon to advance supplier transparency. Engaging supplier companies in discussions about transparency will be essential.
- Together, the coronavirus pandemic, declines in commodity prices and the global economic downturn present major disruptions for supplier firms and will likely precipitate structural change of many supplier markets. This creates urgent incentives for governments and the private sector to improve supply chain resilience and keep production costs low, while making sure that procurement decision making continues to contribute toward a social license to operate. Given these high stakes, it is imperative that governments, the private sector and civil society improve oversight of the roles that supplier firms play in extractive industry projects.

## Introduction

Large oil, gas and mining projects are usually associated with a few big names such as Shell, Exxon, Rio Tinto, Gazprom and Codelco. These are rights holders—companies that receive licenses from host governments to extract resources. Typically, however, lower-profile companies do much of the work to take natural resources out of the ground. These are suppliers—companies that provide the goods and services that make extraction happen. They range in size from multi-billion-dollar international conglomerates like Halliburton, Schlumberger and Caterpillar, to specialized or local firms that may only have a handful of employees.

In recent years, annual spending on extractive sector suppliers averaged nearly a trillion dollars per year. At this scale, spending on suppliers substantially affects how much profit and taxable income the extractive industries generate and provides an important opportunity for countries to build local content. It also presents a chance for corrupt interests to profit. In some places, exposed supplier corruption schemes have rocked world headlines. In Brazil, the sprawling Lava Jato scandal—which implicated several major figures from the business and political elite including three former presidents—pivoted on inflated supplier contracts awarded by national oil company Petrobras. In another scandal, a Monaco-based intermediary called Unaoil facilitated millions of dollars in bribes to officials in multiple countries to help as many as 11 oilfield services and construction companies win lucrative supplier contracts.<sup>1</sup>

At the time of publication, the coronavirus pandemic is disrupting project supply chains in multiple ways. Lockdowns, quarantines and social distancing practices are resulting in delays, cancelations and shortages of goods and services and are increasing supplier costs. At the same time, global plunges in oil prices and the values of most minerals and metals have led rights holder companies to slash 2020 spending by as much as 25 percent in the petroleum sector and 20 per cent in the mining sector according to industry estimates.<sup>2</sup> Supplier firms are likely to be hit hard and structural changes are inevitable in many supplier markets.<sup>3</sup> Together with the energy transition away from fossil fuels, these forces create urgent incentives for governments and the private sector to improve supply chain resilience and keep production costs low, while making sure that procurement decision making continues to contribute toward a social license to operate.

- 1 Alexandra Gillies. *Crude Intentions: How Oil Corruption Contaminates the World*, (Oxford University Press, 2020), 38-42, 80-93; Jonathan Watts, "Operation Car Wash: Is this the biggest corruption scandal in history?," *The Guardian*, 1 June 2017, [www.theguardian.com/world/2017/jun/01/brazil-operation-car-wash-is-this-the-biggest-corruption-scandal-in-history](http://www.theguardian.com/world/2017/jun/01/brazil-operation-car-wash-is-this-the-biggest-corruption-scandal-in-history); Paul Caruana Galizia, "Greasing the wheels," *Tortoise*, 14 September 2019, [members.tortoisemedia.com/2019/09/14/sfo-ahsani-190914/content.html](http://members.tortoisemedia.com/2019/09/14/sfo-ahsani-190914/content.html).
- 2 Rystad Energy (2020), *Global OFS demand is set for a 25% decline in 2020. Here is how the recovery will unfold*, Free Markets, 19 March 2020; PwC (2020), *Mine 2020*, 28, [www.pwc.com/mine](http://www.pwc.com/mine); Ron Bousso, "Graphic: Oil majors cut 2020 spending by 22% after prices slump," Reuters, 1 April 2020, [www.reuters.com/article/us-global-oil-majors-capex-graphic/graphic-oil-majors-cut-2020-spending-by-22-after-prices-slump-idUSKBN21J516](http://www.reuters.com/article/us-global-oil-majors-capex-graphic/graphic-oil-majors-cut-2020-spending-by-22-after-prices-slump-idUSKBN21J516); "CHART: Mining's covid-19 capital spending cuts top \$6bn," Mining.com, 20 May 2020, [www.mining.com/chart-minings-covid-19-capital-spending-cuts](http://www.mining.com/chart-minings-covid-19-capital-spending-cuts).
- 3 For example, Rystad Energy estimates that more than a third of oil field service providers will be unable to meet their interest payment obligations in 2020. Rystad Energy (2020), *High waves to the danger zone: oil service players face debt defaults*, Service Analytics, 19 March 2020.

Despite these high stakes, few governments and rights holders publish detailed information on the roles suppliers play and their economic impacts. As a result, the allocation of supplier contracts and the regulation of supplier activities often takes place with only limited oversight from a small set of industry insiders. Where external oversight is weak, potential risks include:

- Cost overruns that undermine company profits and government revenues
- Failures to tax supplier profits in optimal ways, resulting in lost tax revenues
- Underqualified firms undertaking crucial operations
- Local procurement procedures that fail to create robust economic linkages with the broader domestic economy while allowing well-connected elites to benefit disproportionately

This report makes the case for greater oversight of extractive industry suppliers. In the sections that follow, we explain the economic significance of extractive industry suppliers and identify the main stakeholders involved in supplier governance. We then consider four policy areas where the impacts of poor supplier governance play out: cost control, supplier tax contributions, local procurement and corruption. As a starting point for further discussion on supplier oversight, we end by reviewing how governments, rights holders, state-owned enterprises (SOEs) and suppliers are beginning to share information on the economic impacts of suppliers, how these disclosures feature in global transparency and reporting initiatives and what more can be done.

The research informing this report draws on a review of literature, laws, policies and standards concerning supplier governance and reporting; analysis of data from commercial platforms maintained by Rystad and S&P; analysis of foreign bribery cases involving suppliers (pursued mainly under the U.S. Foreign Corrupt Practices Act and the U.K. Bribery Act); and interviews with industry players and policy practitioners. We focus on supplier oversight from an economic and integrity perspective. Of course, supplier governance also has well-documented consequences for the environment, social well-being and human rights, but these are beyond the scope of this report.

# Understanding extractive industry suppliers

**When citizens, journalists, and oversight actors talk about companies working on extractive industries projects, they usually consider the highly visible companies that hold the rights to exploit oil, gas and minerals.** These include big international companies, SOEs, and smaller independent and domestic producers. In this report, we refer to these companies as rights holders. However, most extractive industry activities today would not be possible without the range of companies that provide the many goods and services needed to take natural resources out of the ground. In this report we refer to these companies as suppliers.

**Supplier companies are a varied group.** They can be multinational or local, large or small. They may take part in all phases of a project's lifespan or just a part of it.<sup>4</sup> They may serve only the extractive industries or supply other sectors of the economy as well. Some offer limited, specialized goods or services, while others can provide as much as 90 percent of the products needed to explore, develop and produce natural resources.<sup>5</sup> The largest suppliers are generally involved in oilfield services; engineering, procurement and construction (EPC); the provision of equipment and infrastructure; and mining services. (See table 1.) Many suppliers also contract with further suppliers, creating several tiers of transactions. While it is possible to make distinctions between different types of suppliers, including but not limited to contractors, subcontractors, equipment providers and service providers, for the purposes of this report, we treat them all under the umbrella term "suppliers."

*Most extractive industry activities today would not be possible without the range of supplier companies that provide the many goods and services needed to take natural resources out of the ground.*

## WHAT'S AT STAKE? SPENDING ON SUPPLIERS

**Suppliers receive a major share of the gross revenues generated by extractive industry projects worldwide.** Using industry data we estimate that between 2000 and 2017 cumulative spending by rights holders on suppliers was equivalent to a quarter of the money generated by petroleum assets and a little under half for mining assets. (See figure 1.) For the upstream extractive industries as a whole, rights holders' spending on suppliers averaged USD 960 billion a year between 2008 and 2017, with suppliers in the petroleum sector receiving USD 800 billion a year and those in the mining sector USD 160 billion annually.<sup>6</sup> (See figure 2.) This

*For the upstream extractive industries as a whole, rights holders' spending on suppliers averaged USD 960 billion a year between 2008 and 2017.*

- 4 Silvana Tordo, Michael Warner, Osmel E. Manzano and Yahya Anouti. Local Content Policies in the Oil and Gas Sector (World Bank, 2013), 161-163; Columbia Center on Sustainable Investment (CCSI), *Linkages to the Resource Sector: The Role of Companies, Government and International Development Cooperation* (2016), [ccsi.columbia.edu/files/2016/07/Linkages-to-the-resource-sector-GIZ-CCSI-2016.pdf](https://ccsi.columbia.edu/files/2016/07/Linkages-to-the-resource-sector-GIZ-CCSI-2016.pdf); J. Korinek. The mining global value chain, (OECD Trade Policy Papers, No. 235, 2020), [www.oecd-ilibrary.org/trade/the-mining-global-value-chain\\_2827283e-en](https://www.oecd-ilibrary.org/trade/the-mining-global-value-chain_2827283e-en).
- 5 Valérie Marcel, Alan Kennedy and Zoe Thompson. "Unsung Workhorses of the Oil Industry - Oilfield Service Companies," KPMG, 2016, 3, [assets.kpmg/content/dam/kpmg/pdf/2016/03/oilfield-services-companies-unsung-workhorses-oil-industry.pdf](https://assets.kpmg/content/dam/kpmg/pdf/2016/03/oilfield-services-companies-unsung-workhorses-oil-industry.pdf).
- 6 Rystad Energy: EP expenditure by service segment and S&P Global: Mine Economics. We note that these findings complement other estimates published by Olle Östensson. Local content, supply chains, and shared infrastructure, (UN-WIDER, 2017), 2, [www.wider.unu.edu/sites/default/files/wp2017-96.pdf](https://www.wider.unu.edu/sites/default/files/wp2017-96.pdf); International Council of Mining and Minerals, *Taxation and other economic benefits*, [www.icmm.com/en-gb/society-and-the-economy/economic-development/taxation](http://www.icmm.com/en-gb/society-and-the-economy/economic-development/taxation); and World Gold Council, *Socio-Economic Impact of Mining Gold* (2015), [www.gold.org/goldhub/research/socio-economic-impact-mining-gold](http://www.gold.org/goldhub/research/socio-economic-impact-mining-gold).

spending included both capital expenditures, such as facilities development, and operational expenditures, such as operations and maintenance. We include more information on how we calculated these figures in the appendix.

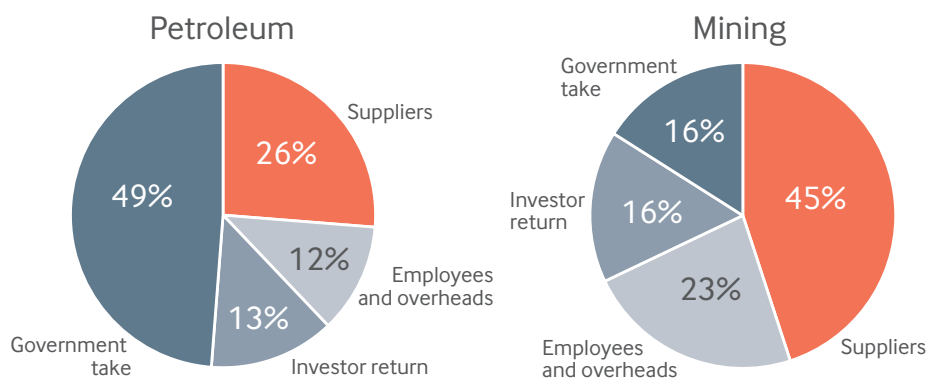


Figure 1. Distribution of gross revenues generated by extractive industries, cumulative 2000 to 2017<sup>10</sup>

**While multiple factors affect spending on suppliers, outlays correlate closely with commodity prices.**<sup>7</sup> From a peak of USD 1.2 trillion in 2014, rights holders’ estimated spending on suppliers dropped beneath USD 800 billion by 2016 as prevailing prices for oil and many minerals plummeted. (See figure 2.) Likewise, as the coronavirus pandemic has precipitated rapid falls in many commodity prices in 2020, rights holders’ spending on suppliers has already declined sharply as they have moved quickly to slash expenditures.<sup>8</sup> Other factors that influence spending on suppliers include project location, profitability and phase of development, as well as company practices vis-à-vis outsourcing.<sup>9</sup> Given its scale, spending on suppliers is a major determinant of how much profit, taxable income and local procurement opportunities the extractive industries generate.

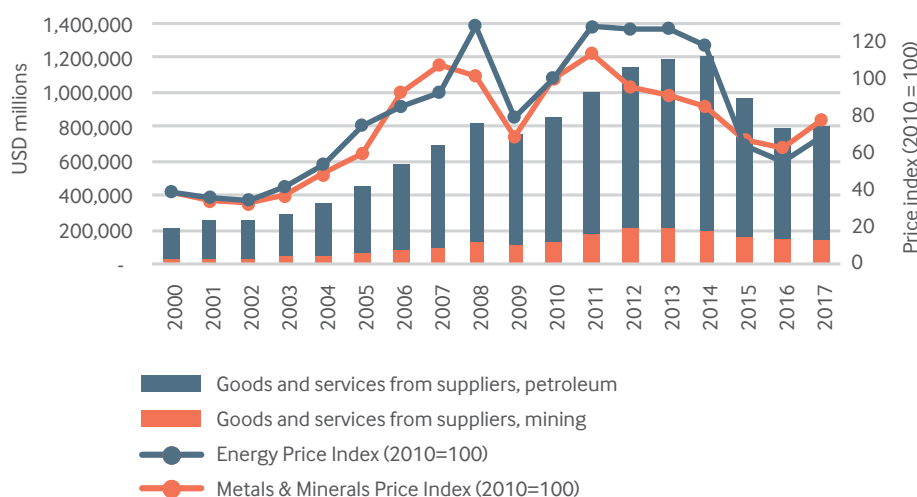


Figure 2. Rights holders’ annual spending on suppliers, 2000 to 2017, nominal USD<sup>11</sup>

7 G. Toews and A. Naumov. *The Relationship Between Oil Price and Costs in the Oil and Gas Sector*, Working Paper (OxCarre, 2015), [www.economics.ox.ac.uk/materials/papers/13819/paper152.pdf](http://www.economics.ox.ac.uk/materials/papers/13819/paper152.pdf).  
 8 Rystad Energy (2020), *Global Service Report April 2020*.  
 9 CCSI, *Linkages to the Resource Sector*, 20-22.  
 10 Authors’ estimates using data from *Rystad Energy: EP expenditure by service segment* and *S&P Global: Mine Economics*. (See appendix for notes on how we calculated these estimates.)  
 11 *Ibid.*

Supplier category	Company name (relevant business line if applicable)	Country of headquarters	2018 revenue (USD billion)
Oilfield services (OFS)	Schlumberger	United States	33
	Halliburton	United States	24
	Baker Hughes, a GE Company	United States	23
	Weatherford	Switzerland	6
	Petrofac	United Kingdom	6
	China Oilfield Services Limited	China	3
Mining services	CIMIC Group	Australia	11
	FLSmidth	Denmark	3
	Perenti Global	Australia	1
Engineering, procurement and construction (EPC)	Fluor	United States	19
	TechnipFMC	United Kingdom	13
	Saipem	Italy	10
	Hyundai Engineering and Construction	Korea	6
	Worley	Australia	4
Original equipment manufacturers (OEM)	Komatsu (construction, mining and utility equipment)	Japan	25 (22)
	Caterpillar (resource industries)	United States	55 (10)
	Sandvik (mining and rock technology)	Sweden	11 (5)
	Thyssenkrupp (industrial solutions)	Germany	50 (6)

Table 1. Selected major international oil, gas and mining suppliers by category, country of origin and revenue<sup>12</sup>

12 Sourced from 2018 annual reports and public filings.



## WHO IS INVOLVED IN SUPPLIER GOVERNANCE?

**Host country governments set the general parameters under which the business of extraction takes place.**<sup>13</sup> They make the rules that all companies working in the country must abide by on issues such as taxation, corporate governance and ethics, environmental and social protections and health and safety. However, they may be unable to regulate the actions of non-resident suppliers who contribute from a location beyond the host government's jurisdiction. Host governments are also typically responsible for managing natural resources. As such, they issue the licenses and permits that enable rights-holding companies to exploit oil, gas and minerals. While they normally directly oversee rights-holding companies, the degree to which they get involved in supplier governance varies. Some governments, particularly those operating concessionary regimes, take a light touch approach toward supplier oversight, limiting their involvement to post-hoc tax audits of supplier payments. Others carve out more active roles. When countries use production sharing contracts, as is common in the petroleum industry, it is standard practice for the rights holder to produce and submit annual budgets and work plans for government approval. Some governments also play a role in approving certain major supplier contracts, and others encourage or require local spending through local content policies. Finally, governments also engage in oversight via SOEs as described further below.

**Rights holders decide what goods and services they need.** As the companies that hold the legal right to exploit resources, rights holders are ultimately responsible for the outcomes of extractive industry projects. In this role, they take on financial risks, manage relations with host governments and communities, and oversee project supply chains. This involves defining the standards and specifications for goods and services, selecting suppliers, supervising their work and paying them for what they supply. A rights holder may be a single company, or a consortium of companies arranged under a joint venture. Where multiple companies share exploitation rights through a consortium or joint venture, a practice particularly common in the petroleum sector, a single company is usually designated as the "operator" and put in charge of the day-to-day management of the project. Where this is the case, the operator company's supplier management processes usually take precedence, but joint venture or consortium partners may still participate in reviewing and approving budgets, costs and the selection of major suppliers.<sup>14</sup>

13 By "host country" we mean the country where extraction takes place.

14 David Delahay and Karl Schmalz. "Why Upstream Oil and Gas Poses Lower Transfer Pricing Risks Than Other Industries," *Tax Notes International*, 14 January 2019, 181-182, [static1.squarespace.com/static/5a789b2a1f318da5a590af4a/t/5c6452dbe79c7063400536f8/1550078684125/2019tni2-8-Delahay\\_Schmalz.pdf](https://static1.squarespace.com/static/5a789b2a1f318da5a590af4a/t/5c6452dbe79c7063400536f8/1550078684125/2019tni2-8-Delahay_Schmalz.pdf).

**SOEs play a range of complex, overlapping roles vis-à-vis suppliers.** This can include acting as operators, non-operating partners, regulators and even as suppliers. When acting as operators of a given extractive project, they take on all of the rights-holder responsibilities for supplier governance just described. As non-operating partners or representatives of the government, SOEs may be involved in approving major contracts and reviewing costs as part of project joint management committees or other structures. They may also play an active role in other project committees involved in day-to-day supplier selection and approval. As regulators, they may be able to engage in supplier governance in the same ways that host governments do more generally, including setting the rules, monitoring rights holder compliance and by approving key decisions by partner companies regarding exploration and production activities.<sup>15</sup> Some SOEs are recipients of supplier contracts and so may also be suppliers themselves.<sup>16</sup>

**The international community, home country governments, and financiers also wield some influence over supplier governance.** International initiatives and standards, such as the United Nations *Guiding Principles on Business and Human Rights*, the International Finance Corporation's (IFC) *Performance Standards*, the Organisation for Economic Co-operation and Development's (OECD) *Guidelines for Multinational Enterprises*, and the *Financial Action Task Force on Money Laundering Recommendations* have established basic expectations for supply chain due diligence on human rights, the environment and corruption. In the extractives space specifically, the OECD has developed specific due diligence guidance for responsible supply chains of minerals from conflict-affected and high-risk areas. Home countries such as Australia, France, the U.K. and the U.S. have developed laws that require or encourage rights holder and supplier companies to pursue these aims in their compliance, risk management and procurement systems.<sup>17,18</sup> Dozens of financial institutions have adopted the Equator Principles risk management framework as a minimum standard for due diligence to support responsible risk decision-making on environmental and social impacts, while over 2,000 investor groups are signatories to the United Nation's (UN) Principles of Responsible Investment, which seek to incorporate environment, social and governance issues into investment analysis and decision-making processes.

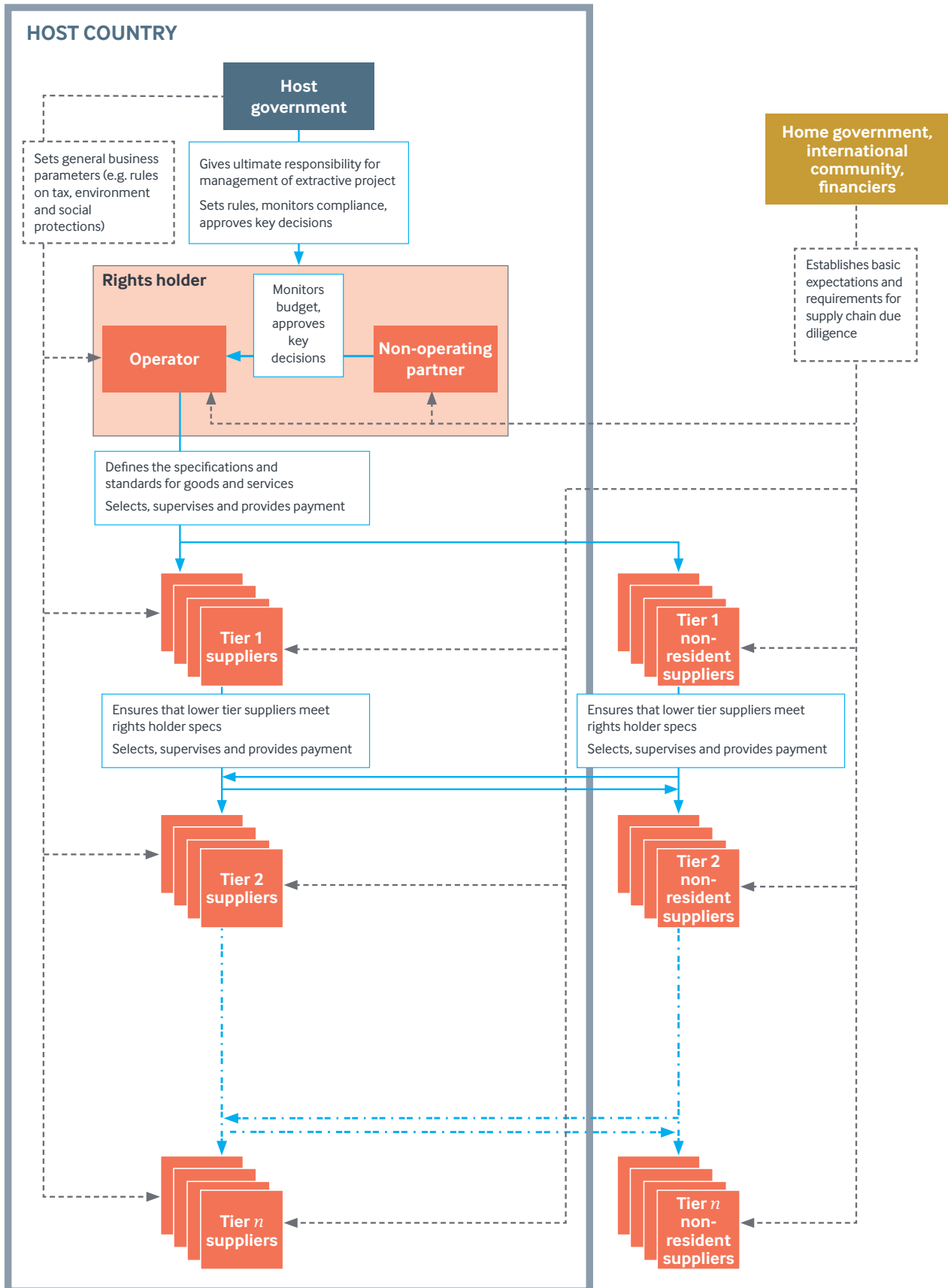
15 Patrick Heller, Paasha Mahdavi and Johannes Schreuder. "Reforming National Oil Companies: Nine Recommendations" (NRGI, 2014), 7. [www.resourcegovernance.org/sites/default/files/documents/nrgi\\_9recs\\_eng\\_v3.pdf](http://www.resourcegovernance.org/sites/default/files/documents/nrgi_9recs_eng_v3.pdf).

16 See for example, China National Petroleum Corporation, CNPC at a Glance: <http://www.cnpc.com.cn/en/cnecatag glance/cnecatag glance.shtml#cnecatag glance>

17 By "home country" we mean a country where a company or investor is resident or incorporated.

18 Examples include U.K. Bribery Act 2010; U.K. Modern Slavery Act 2015; U.S. Foreign Corrupt Practices Act of 1977; U.S. Dodd Frank Wall Street Reform and Consumer Protection Act of 2010, Section 1502 regarding conflict minerals; and the French Loi de Vigilance No. 2017-339 of 2017 among others.

Figure 3. Players involved in supplier governance in the extractives sector



## Four issues in the oversight of suppliers

The sheer scale of spending on suppliers means that supplier governance decisions have important economic impacts for the citizens of resource-rich countries. In what follows, we consider four areas where these impacts play out: cost control, supplier contributions to tax revenues, local procurement and corruption. As we will see, each faces particular oversight challenges, which stem in part from a lack of awareness and attention of the roles that suppliers play in the extractive industries.

### ISSUE 1. COST CONTROL

**Supplier costs carry financial implications for both rights-holding companies and governments. Inflated supplier costs reduce the profits of rights holders and the revenues that governments can tax.**<sup>19</sup> Where the state engages in the sector via SOEs, higher costs can also mean that national companies spend more public money, which can reduce the funds that SOEs are able to transfer into the public treasury. Lower costs and greater profits are of course also in the interest of rights holders, since they can distribute after-tax profit to shareholders or reinvest it. As a result, in most instances rights holders and governments have a shared interest in keeping costs down. Nevertheless, cost control is a common challenge in the extractive industries. A study of megaprojects by EY showed that 64 percent of petroleum projects and 69 percent of mining projects were over budget. And these overruns were big: where cost data was available, the average overrun was 59 percent in the petroleum sector and 62 percent in the mining industry.<sup>20</sup>

*In most instances rights holders and governments have a shared interest in keeping costs down.*

**Oversight on costs, including supplier costs, comes largely from the private sector, with secondary roles for government auditors.** Costs are primarily kept in check by the procurement and contract management systems of rights holders. However, many governments also carry out their own cost audits. This is necessary because there are certain circumstances in which private sector procurement and contract management systems fail to control costs, as well as other situations where government interests do not align with those of rights holders. We explore some of these in box 1.

19 This is particularly pertinent for developing countries, given their greater reliance on corporate income tax. United Nations Conference on Trade and Development, *World Investment Report 2015: Reforming International Investment Governance* (2015), 182, [unctad.org/en/PublicationsLibrary/wir2015\\_en.pdf](http://unctad.org/en/PublicationsLibrary/wir2015_en.pdf).

20 EY, *Spotlight on oil and gas megaprojects*, (2014), 4-6, [www.ey.com/Publication/vwLUAssets/EY-spotlight-on-oil-and-gas-megaprojects/\\$FILE/EY-spotlight-on-oil-and-gas-megaprojects.pdf](http://www.ey.com/Publication/vwLUAssets/EY-spotlight-on-oil-and-gas-megaprojects/$FILE/EY-spotlight-on-oil-and-gas-megaprojects.pdf); EY, *Opportunities to enhance capital productivity: Mining and metals megaprojects* (2017), 3-7, [www.ey.com/Publication/vwLUAssets/EY-opportunities-to-enhance-capital-productivity/\\$FILE/EY-opportunities-to-enhance-capital-productivity.pdf](http://www.ey.com/Publication/vwLUAssets/EY-opportunities-to-enhance-capital-productivity/$FILE/EY-opportunities-to-enhance-capital-productivity.pdf).



**Public information about government cost audits in the extractive industries is sparse, but examples show that they can uncover major losses.**

For example, public audit reports for nine oil permits in the Republic of Congo from 2004 to 2005 found that oil and gas companies overstated their costs by USD 127 million, leading to estimated tax losses of USD 63.5 million. In Uganda, the auditor general disallowed excessive petroleum project costs amounting to USD 81 million for the period 2004 to 2011, which otherwise could have decreased government revenue by USD 24 million.<sup>21</sup>

**Government oversight actors and the wider public often misunderstand supplier roles and cost auditing processes. This creates an accountability gap.** As noted by Oxfam in a study on cost auditing in the petroleum sector, while supreme audit institutions and legislatures usually have official powers to provide assurance and scrutiny over government cost audit processes, few do because they lack the industry knowledge or political support required to provide effective monitoring.<sup>22</sup> This state of affairs is further reinforced by similar knowledge gaps in civil society and the media.

**While it is neither possible nor advisable for actors outside government to undertake cost audits, greater knowledge, understanding and public debate about spending on suppliers and government cost audit processes could be helpful in two ways.** First, it would help official oversight actors such as parliamentarians, anti-corruption authorities, the media and civil society to know whether governments are making effective use of their audit rights. Second, it might help draw attention to particular challenges that prevent the effective application of audits, such as gaps or loopholes in the law, capacity issues in agencies carrying out audits, or even corruption. SOE audits are especially important, as these companies may have less effective internal controls or non-independent audit committees and, in certain cases, less pressing incentives to maximize profits.<sup>23</sup>

21 Daniel Mulé, Alexandra Readhead and Anton Op de Beke. *Examining the crude details* (Oxfam, 2018), 5-6, [www.oxfam.org/en/research/examining-crude-details](http://www.oxfam.org/en/research/examining-crude-details).

22 *Ibid.*, 46-48.

23 OECD, *Guidelines on Anti-Corruption and Integrity in State-Owned Enterprises* (2019), [www.oecd.org/daf/ca/Guidelines-Anti-Corruption-Integrity-State-Owned-Enterprises.pdf](http://www.oecd.org/daf/ca/Guidelines-Anti-Corruption-Integrity-State-Owned-Enterprises.pdf).

### Box 1. Where efforts to control costs may fall short

Rights holders can struggle to control costs in at least the following circumstances:

- 1 **Rights holders have limited negotiating power to keep down costs.** Some supplier market segments have only a limited number of competitors. Monopolies or oligopolies improve the negotiating power of suppliers, allowing them to set prices. Illustrating the dominant position of some companies, the U.S. Department of Justice's 2016 decision to reject the proposed merger between Halliburton and Baker Hughes noted that together with Schlumberger, they controlled approximately 94 percent of the U.S. offshore directional drilling services market.<sup>24</sup> While many markets remain fragmented, there has been some consolidation in oilfield services since the 2014 commodity price downturn, leaving rights holders with fewer choices.<sup>25</sup> In other cases, rights holders can also be reluctant to replace suppliers with whom they have a long history of collaboration through shared technology and information, or joint research and development, even if a more cost-effective alternative is available elsewhere.<sup>26</sup>
- 2 **Rights holders or their suppliers buy or lease goods and services from related parties.** While the practice of using related party suppliers is common, it can take an abusive form. Through transfer mispricing, companies can intentionally inflate fees paid to related companies in order to transfer taxable profits from host countries to low-tax jurisdictions or to facilitate other kinds of fraud.<sup>27</sup> In Zambia, for example, the Zambia Financial Intelligence Center suspected that the foreign CEO of a large foreign mining company was deliberately overpaying for services to reduce his company's taxes by shifting profits to companies based in his home country in which he had an interest. In contracts facilitated by the CEO, the mining company gave work to Zambian suppliers, who then paid exorbitant "management fees" to the foreign companies from the CEO's home country, while subcontracting the actual work to other local firms at a fraction of the original cost. In one instance, one Zambian company received ZMW 7 million for works valued at less than ZMW 100,000.<sup>28</sup>
- 3 **Suppliers control or invest capital in extractive industry projects.** Since 2014, when the commodities downturn cut demand for supplier products, some large suppliers have been using their own investments to stimulate demand. This creates another source of related party concerns. Schlumberger has been a pioneer in this area, with its production management division holding investments of USD 2.6 billion as of June 2017.<sup>29</sup> Elsewhere, Petrofac's integrated energy services division has also started offering risk service contracts under which it takes up-front capital risks in projects.<sup>30</sup> Meanwhile in Guinea, the rights holder for the country's bauxite mine with the highest output, the SMB Winning consortium, is owned by three major subcontractors for the project: Singapore's Winning Shipping Ltd., a shipping company; UMS, a Guinean transportation and logistics company; and the China Hongqiao Group.<sup>31</sup>

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24 U.S. DOJ v. Halliburton Co., and Baker Hughes Inc., Case 1:16-cv-00233-UNA (2016), 7, [www.justice.gov/atr/file/838661/download](http://www.justice.gov/atr/file/838661/download).

25 Significant mergers and acquisitions include Schlumberger's 2016 acquisition of Cameron, the 2017 mergers of FMC Technology and Technip, and Baker Hughes and GE Oil & Gas. See Deloitte, "Phoenix Rising: the Oil Field Services Sector Transforms Again" (2017), 19, [www2.deloitte.com/content/dam/Deloitte/us/Documents/energy-resources/us-er-OFS-oilfield-services\\_transformation.pdf](http://www2.deloitte.com/content/dam/Deloitte/us/Documents/energy-resources/us-er-OFS-oilfield-services_transformation.pdf).

26 Research interviews.

27 Alexandra Readhead, *Preventing Tax Base Erosion in Africa* (NRGI, 2016), 2, [resourcegovernance.org/sites/default/files/documents/nrgi\\_transfer-pricing-study.pdf](http://resourcegovernance.org/sites/default/files/documents/nrgi_transfer-pricing-study.pdf).

28 Zambia Financial Intelligence Centre, Trends Report (2016), 24-26, [www.fic.gov.zm/79-fic-news/98-trends-report-2016](http://www.fic.gov.zm/79-fic-news/98-trends-report-2016).

29 Liz Hampton, "The next oil major? Service firm Schlumberger's big bet on production," Reuters, 2016, [www.reuters.com/article/us-schlumberger-oil-production-insight/the-next-oil-major-service-firm-schlumbergers-big-bet-on-production-idUSKCN1BJ0EI](http://www.reuters.com/article/us-schlumberger-oil-production-insight/the-next-oil-major-service-firm-schlumbergers-big-bet-on-production-idUSKCN1BJ0EI).

30 Marcel et al, *Unsung Workhorses of the Oil Industry*, 6.

31 See About Consortium, *SMB-Winning*, [www.smbwinning.com/en/about-consortium/](http://www.smbwinning.com/en/about-consortium/)

**4 Aims other than maximizing commercial returns drive procurement and spending decisions.** Not all procurement decisions are driven by a profit motive. Many SOEs and rights holders sometimes sacrifice efficient procurement in favor of delivering employment, local business opportunities and other in-country benefits.<sup>32</sup> At the same time, favoritism, corruption and mismanagement are also problems that can lead to inflated costs. In Indonesia, for example, an audit found that the national oil company Pertamina, lost USD 6 billion between 1996 and 1998 due to “embezzlement, illegal commissions, price mark-ups on procurement contracts, gross inefficiency and incompetence.”<sup>33</sup> A U.S. anti-bribery investigation alleged that a bribery scheme in Angola involving oil-field services company Weatherford allowed the company to win contracts for which its prices were 30 percent higher than the competition.<sup>34</sup>

## ISSUE 2. SUPPLIER CONTRIBUTION TO TAX REVENUES

**Profits made by suppliers may represent an important tax base in some countries.** However, the cross-border, short-term and intangible nature of much supplier work can make it hard for resource-rich countries to tax them optimally. Some governments also choose to grant exemptions from taxes related to suppliers. These can drive down overall project costs and increase profitability but in some instances they may result in the government failing to capture resource rents that accrue with suppliers. These issues may have important consequences for public finances but they are rarely considered in public debates on extractive industry taxation. Nevertheless, some tax authorities have started looking more closely at taxing extractive industry suppliers.<sup>35</sup>

*The cross-border, short-term and intangible nature of much supplier work can make it hard for resource-rich countries to tax them optimally.*

**Governments face strategy and administration challenges when taxing suppliers.** Many of these difficulties relate to taxing non-resident companies.<sup>36</sup> In theory, governments should only tax companies on profits made and goods and services supplied and consumed in the host state. While this is relatively straightforward to determine for local companies, several issues arise with non-resident suppliers. In the first instance, tax administrators must determine whether a supplier’s presence reflects a “permanent establishment,” which would make the company liable for corporate taxation at the local rate. Given that many suppliers provide services from multiple jurisdictions under short-term contracts, this can be challenging. Moreover, even in instances where a supplier is working under a

32 Patrick Heller and David Mihalyi. *Massive and Misunderstood: Data-Driven Insights into National Oil Companies* (NRGI, 2019), 4, [www.nationaloilcompanydata.org/api/publications/content/BWEOxwl3qpbpPk5RkZmWr3g5TEvNgLD4LD21foHP.pdf](http://www.nationaloilcompanydata.org/api/publications/content/BWEOxwl3qpbpPk5RkZmWr3g5TEvNgLD4LD21foHP.pdf)

33 Andrew Bauer (2018), *Upstream Oil, Gas and Mining State-Owned Enterprises: Governance Challenges and the Role of International Reporting Standards in Improving Performance*, p.21-23, [eiti.org/document/upstream-oil-gas-mining-soe-governance-challenges](http://eiti.org/document/upstream-oil-gas-mining-soe-governance-challenges)

34 U.S. DOJ v. Weatherford Services LTD., Case 4:13-cr-00734, Plea Agreement, Statement of Facts, 9, [www.justice.gov/sites/default/files/criminal-fraud/legacy/2013/11/26/Weatherford-Services-Plea-Agreement.pdf](http://www.justice.gov/sites/default/files/criminal-fraud/legacy/2013/11/26/Weatherford-Services-Plea-Agreement.pdf)

35 For example, the Australian Tax office recently expanded a probe into Schlumberger’s activities. In 2015, it also ordered the company to pay AUS 51 million to settle a transfer pricing claim. See Peter Ker, “ATO expands probe into oilfield services giant Schlumberger,” *Financial Review*, 8 May 2018, [www.afr.com/companies/energy/ato-expands-probe-into-oilfield-services-giant-schlumberger-20180508-h0zs3a](http://www.afr.com/companies/energy/ato-expands-probe-into-oilfield-services-giant-schlumberger-20180508-h0zs3a); Peter Ker, “Oil contractor Schlumberger to pay \$51m to settle ATO ‘transfer pricing’ claim,” *Sydney Morning Herald*, 19 Jul 2015, [www.smh.com.au/money/tax/oil-contractor-schlumberger-to-pay-51m-to-settle-ato-transfer-pricing-claim-20150717-gif426.html](http://www.smh.com.au/money/tax/oil-contractor-schlumberger-to-pay-51m-to-settle-ato-transfer-pricing-claim-20150717-gif426.html).

36 United Nations Department for Economic and Social Affairs, *Handbook on Extractive Industry Taxation by Developing Countries* (2017), 58, [www.un.org/esa/ffd/wp-content/uploads/2018/05/Extractives-Handbook\\_2017.pdf](http://www.un.org/esa/ffd/wp-content/uploads/2018/05/Extractives-Handbook_2017.pdf).

permanent establishment, tax administrators still need to determine where the services were provided and what portion of the income their state should tax.

**Given these challenges, governments often rely on withholding taxes (WHTs) to tax non-resident suppliers.** These are taxes levied by a host country on certain types of payments made to overseas companies. Technically, WHT is levied on the overseas company that receives the payment, but “withheld” by the locally-resident company sending the payment, which may be the rights holder or even a locally-registered supplier that has contracted another overseas supplier.<sup>37</sup> WHT allows the government to collect some tax from suppliers that do not have permanent establishment, but it can present its own risks. Most importantly, some suppliers may build WHT payments into their fees, thereby increasing rights holder costs, in turn decreasing profits subject to tax. And because WHT does not consider supplier profits or costs, it is not a particularly sophisticated tax tool.<sup>38</sup>

**More generally, important questions remain about whether host countries should include suppliers in their efforts to tax resource rents—that is, profits that are above and beyond normal economic returns.**<sup>39</sup> How to effectively tax resource rents is perhaps the most crucial question when it comes to extractive industry taxation. In theory, procurement and cost control mechanisms should keep supplier margins small, which would mean that suppliers capture little in the way of resource rents. However, in situations where rights holders and governments do not effectively control supplier costs (see previous section), resource rents may accumulate with supplier companies. In these cases, governments must be able to tax supplier profits or improve cost controls and avoid rent distribution further down the supply chain.

**Tax exemptions for suppliers are common.** Investors argue that tax exemptions for suppliers make projects more efficient, reducing costs and allowing for greater project profits and tax gains elsewhere. Governments may write these types of exemptions into laws, their contracts with rights holders or bilateral tax treaties.<sup>40</sup> They may affect WHT payments to non-resident suppliers, thresholds for permanent establishment and other taxes such as import duties and value added tax (VAT).

*In situations where rights holders and governments do not effectively control supplier costs, resource rents may accumulate with supplier companies.*

37 Martin Hearson. *Tax treaties in sub-Saharan Africa: a critical review* (Tax Justice Network, 2015), 17, [eprints.lse.ac.uk/67903/1/Hearson\\_Tax\\_treaties\\_in\\_sub-Saharan\\_Africa.pdf](https://eprints.lse.ac.uk/67903/1/Hearson_Tax_treaties_in_sub-Saharan_Africa.pdf).

38 WHTs are highly regressive, meaning that they take a larger percentage of income from suppliers with low margins than from those with high margins. United Nations Department for Economic and Social Affairs, Handbook on Extractive Industry Taxation by Developing Countries; interviews with industry practitioners.

39 NRGI, Natural Resource Charter (2014), Precept 4, [www.resourcegovernance.org/sites/default/files/documents/nrcj1193\\_natural\\_resource\\_charter\\_19.6.14.pdf](http://www.resourcegovernance.org/sites/default/files/documents/nrcj1193_natural_resource_charter_19.6.14.pdf).

40 For information on legal and contractual tax incentives in the mining sector, including exemptions for suppliers, see Intergovernmental Forum on Mining, Minerals, Metals and Sustainable Development, Insights on Incentives: Tax competition in mining (2019), [www.iisd.org/sites/default/files/publications/insights-incentives-tax-competition-mining.pdf](http://www.iisd.org/sites/default/files/publications/insights-incentives-tax-competition-mining.pdf). For contractual tax incentives for suppliers in the petroleum sector see the following public domain contracts on the global Resource Contracts repository, [www.resourcecontracts.org](http://www.resourcecontracts.org): Talisman (Block K39) B.V., Topkhana Block, PSA, 2011 (Iraq), section 31.4; Kulob Petroleum Limited, PSA, 2008 (Tajikistan), Section 17.2; Model Contract (English), Guinea Ecuatorial de Petroleos, PSA, 2019, (Equatorial Guinea), Section 14. For information on incentives in tax treaties see M. Hearson. The ActionAid Tax Treaties Dataset (Institute of Development Studies, 2016), [www.ictd.ac/dataset/action-aid-tax-treaties-dataset](http://www.ictd.ac/dataset/action-aid-tax-treaties-dataset).



**While there may be good reasons for exemptions, their impacts should be scrutinized.** First, supplier tax flows can provide governments with immediate revenues. Cash-strapped governments do not have to wait for production to start or for companies to recover their costs. At the same time, badly designed exemptions can discriminate against certain companies. In particular, exemptions that only cover international or non-resident suppliers can put local companies at a disadvantage and undermine local content ambitions.<sup>41</sup> Finally, supplier tax exemptions can be large. In Guyana, for example, the Stabroek block contract exempts all WHT payments to subcontractors or affiliated companies during the exploration period.<sup>42</sup> Given Rystad estimates that operator ExxonMobil spent USD 4.58 billion on exploration in the block through the end of 2019, we estimate that exempted WHT up to this date could be more than a hundred million dollars.<sup>43</sup> This does not mean that Guyana lost a hundred million dollars: given the tradeoffs between different sources of taxation, any assessment of revenues needs to be viewed holistically. In this case for example, having to pay WHT could have impacted project profitability and so reduced revenues from other profit-based taxes over the life of the project.

**Supplier taxation issues take a low profile in most public debates on extractive industry taxation.** Publicly available models developed to support tax decision-making, such as those produced by international institutions, non-governmental organizations (NGOs) and think tanks, generally do not consider these issues in detail.<sup>44</sup> Suppliers themselves also rarely engage in extractive industry tax reporting processes such as the Extractive Industries Transparency Initiative (EITI). If host governments disclosed the tax contributions of suppliers and communicated the government's strategy for taxing supplier profits, stakeholders could better assess the chosen policies based on evidence and data, and then exercise more oversight of how the government implements them.

41 Kaisa Toroskainen and Herve Lado. "EITI Data Can Support Guinea's Efforts to Promote Local Mining Subcontractors" (NRGI, 2019), [www.resourcegovernance.org/blog/eiti-data-guinea-mining-subcontractors-local-content](http://www.resourcegovernance.org/blog/eiti-data-guinea-mining-subcontractors-local-content).

42 Esso Exploration and Production Guyana Ltd, CNOOC Nexen Petroleum Guyana Ltd, Hess Guyana Exploration Ltd, PSA, 2016, Section 15.10, [www.resourcecontracts.org/contract/ocds-591adf-1399550295/view-/search/15.10](http://www.resourcecontracts.org/contract/ocds-591adf-1399550295/view-/search/15.10).

43 This estimate is based on the following considerations: (1) Rystad estimates showing that USD4.56 billion was spent on exploration in the field to end 2019 and an assumption that the contractual withholding tax exemption applies throughout this period; (2) Rystad data showing that the percentage of petroleum industry expenditures that go to suppliers is on average over two thirds; (3) An assumption of a 10 percent withholding tax (Guyana's standard withholding tax rates are 20 percent, while Guyana's tax treaties with the U.K. and Canada cap taxes on technical fees and management fees at 10 percent; EY, Global Oil and Gas Tax Guide (2019), 266, [www.ey.com/Publication/vwLUAssets/ey-global-oil-and-gas-tax-guide-2019/\\$FILE/ey-global-oil-and-gas-tax-guide-2019.pdf](http://www.ey.com/Publication/vwLUAssets/ey-global-oil-and-gas-tax-guide-2019/$FILE/ey-global-oil-and-gas-tax-guide-2019.pdf); UK/Guyana Double Taxation Convention (1992), Section 14.2, [assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/498358/guyana\\_DTC\\_-\\_in\\_force.pdf](http://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/498358/guyana_DTC_-_in_force.pdf); Canada-Guyana Income Tax Convention (1985), Section 13.2, [www.canada.ca/en/departement-finance/programmes/tax-policy/tax-treaties/country/guyana-convention-1985.html](http://www.canada.ca/en/departement-finance/programmes/tax-policy/tax-treaties/country/guyana-convention-1985.html)). (4) An assumption that at least 40 percent of expenditures go to non-resident suppliers who do not have a "permanent establishment" in Guyana. Rystad data is from Rystad Energy: U Cube economic model.

44 See, for example, the IMF's Fiscal Analysis of Resource Industries (FARI) model, which is commonly used international institutions and independent analysts as the starting point for building fiscal models for extractive industry projects. [www.imf.org/external/np/fad/fari/](http://www.imf.org/external/np/fad/fari/)

### ISSUE 3. LOCAL PROCUREMENT

**Supplier contracts represent a major channel for local economic benefits.**

“Local content” is the value that an extractive industry project brings to the local, regional or national economy beyond resource revenues.<sup>45</sup> When foreign companies hire more local suppliers, they can help create jobs, businesses and private wealth. Rights holders and international suppliers can also use procurement to transfer valuable skills and technologies to local businesses.<sup>46</sup> Research suggests that local procurement is one of the most effective ways to build economic linkages between extractive projects and the wider economy.<sup>47</sup>

**More and more governments are including local procurement requirements in laws and policies.**<sup>48</sup> Common “demand side” approaches include reserving the provision of certain goods and services for local suppliers; setting targets for local procurement by rights holders; requiring rights holders to develop local procurement plans that the government must approve; and offering tax or other incentives. “Supply side” interventions on the other hand include requiring or incentivizing rights holders to transfer technology and skills; setting up supplier development programs; rolling out schemes to improve the matching of buyers and sellers through government supplier portals; and supporting local firms through financing.<sup>49</sup>

**Companies, too, can have good reasons for procuring locally.** Engaging suppliers located closer to where the extraction takes place can be more cost effective. It can also help the company access context-specific expertise and secure a social license to operate. As a result, many rights holders and some large suppliers have set their own targets for local procurement and are supporting local companies through training and supplier development programs beyond what government policy or laws require.

**Despite this potential, local procurement initiatives often fail to deliver the expected upsides.** A wealth of literature describes the economic and policy challenges. Governance, monitoring and oversight issues are also receiving more attention as countries move from policymaking to implementation.<sup>50</sup> (See box 2 for specific examples.) Among the challenges are:

- **Definitions of “local” can have unintentional negative consequences, as can the chosen implementation targets.** There are many ways to define “local.”<sup>51</sup> A good definition will reflect what the government wants to achieve.

45 NRG, Primer: Local Content (2015), 1, [www.resourcegovernance.org/sites/default/files/documents/nrgi\\_primer\\_local-content.pdf](http://www.resourcegovernance.org/sites/default/files/documents/nrgi_primer_local-content.pdf).

46 Tordo et al., *Local Content Policies in the Oil and Gas Sector*, 161-163.

47 See, for example, Mike Morris, Raphael Kaplinsky, and David Kaplan. One Thing Leads to Another: Promoting Industrialization by Making the Most of the Commodity Boom in Sub-Saharan Africa (2013), [www.researchgate.net/publication/279475209\\_One\\_thing\\_leads\\_to\\_anothercommodities\\_-\\_linkages\\_and\\_industrial\\_development\\_a\\_conceptual\\_overview](http://www.researchgate.net/publication/279475209_One_thing_leads_to_anothercommodities_-_linkages_and_industrial_development_a_conceptual_overview).

48 “It is estimated that 90% of resource-rich countries have adopted a form of local content policy, and increasing local content is a high priority among these governments.” EITI Secretariat, *EITI and Opportunities for Increasing Local Content Transparency* (2019), 3, [eiti.org/files/documents/brief\\_on\\_eiti\\_and\\_local\\_content\\_transparency\\_-\\_formatted.pdf](http://eiti.org/files/documents/brief_on_eiti_and_local_content_transparency_-_formatted.pdf).

49 The International Institute for Sustainable Development, *Local Content Policies in the Mining Sector: Scaling up Local Procurement* (2018), 12-23, [www.iisd.org/sites/default/files/publications/local-content-policies-mining.pdf](http://www.iisd.org/sites/default/files/publications/local-content-policies-mining.pdf).

50 See, for example, Tordo et al. *Local Content Policies in the Oil and Gas Sector*; The International Institute for Sustainable Development, *Local Content Policies in the Mining Sector*.

51 These include geographical definitions ranging from community-based suppliers to national or even regional. Local can also follow from local registration, or a level of local ownership, employment, management personnel, etc. NRG, “Localizing Tanzania’s Gas Sector: Determining Optimal Policies for an Emerging Producer” (2019), 10-11, [www.resourcegovernance.org/analysis-tools/publications/](http://www.resourcegovernance.org/analysis-tools/publications/)

For example, a policy that aims to increase manufacturing should emphasize local value added. One that focuses on jobs for nationals should include employment thresholds. Policies supporting community-based suppliers should emphasize subnational geography. Governments and companies also need to base their targets on realistic assessments of supplier capacity. Poorly crafted definitions and targets can have unintended consequences such as higher costs or deindustrialization. They can also encourage “fronting,” a practice under which companies with a local owner or address receive contracts and then cede benefits or decision-making power to individuals who are not the intended beneficiaries of the local content policy.<sup>52</sup>

- **Political or economic elite interests may influence local procurement.** Given how much money is at stake, local procurement offers local economic elites a mechanism to accumulate wealth.<sup>53</sup> This can happen when certain well-connected actors influence local procurement rules and policies, or when they interfere in contract award processes. Companies can also hand out contracts to buy political or community support. Knowing the complexity of the interests at play, many countries set up an independent body to monitor and enforce compliance with local content rules.<sup>54</sup> Some prequalify and approve companies eligible for local procurement contracts. While government local content bodies can make for better implementation, they also introduce another level of discretion and potential interference. Public oversight is critical to ensuring they do not abuse their powers.<sup>55</sup>

*Given how much money is at stake, local procurement offers local economic elites a mechanism to accumulate wealth.*

**Public oversight, transparency and local procurement reporting have lagged behind other areas of the extractive industries.** Strengthening oversight is important for avoiding challenges like those discussed above. Measuring and reporting on local procurement allows governments, local companies and citizens to raise questions about implementation. Publishing information about award processes and outcomes helps local companies learn about opportunities and makes it easier for oversight actors to deter and detect undue influence. Otherwise, local businesses and citizens may come to think that the best supplier deals go to international companies and well-connected locals.<sup>56</sup> One civil society interviewee in Lebanon summed up this frustration, saying, “We know that procurement is taking place, but we don’t know why certain companies and not others are being invited to participate in specific bids, and we are naturally very skeptical.”<sup>57</sup>

localizing-tanzania-gas-sector-determining-optimal-policies-emerging.

52 Ana Maria Esteves, Bruce Coyne and Ana Moreno. *Local Content Initiatives: Enhancing the Subnational Benefits of the Oil, Gas and Mining Sectors* (NRGI, 2013), 8, [www.resourcegovernance.org/sites/default/files/Sub\\_Enhance\\_Benefits\\_20151125.pdf](http://www.resourcegovernance.org/sites/default/files/Sub_Enhance_Benefits_20151125.pdf).

53 Jesse Salah Ovadia. “The Role of Local Content Policies in Natural Resource-Based Development,” (2015), 43, [www.oefse.at/fileadmin/content/Downloads/Publikationen/Oepol/Artikel2015/Teil1\\_03\\_Ovadia.pdf](http://www.oefse.at/fileadmin/content/Downloads/Publikationen/Oepol/Artikel2015/Teil1_03_Ovadia.pdf).

54 *Ibid.*, 43.

55 Jesse Salah Ovadia. “Local Content and Natural Resource Governance: The Cases of Angola and Nigeria,” *The Extractive Industries and Society* (2014) 26, [eprint.ncl.ac.uk/file\\_store/production/205976/93ECC058-DE0D-4AA8-93BA-01412A533FFA.pdf](http://eprint.ncl.ac.uk/file_store/production/205976/93ECC058-DE0D-4AA8-93BA-01412A533FFA.pdf).

56 Engineers without Borders Canada and Canadian International Resource and Development Institute, *The Relationship between Local Procurement Strategies of Mining Companies & their Regulatory Environments* (2017), 16, 40, [www.cirdi.ca/project/the-relationship-between-local-procurement-strategies-of-mining-companies-their-regulatory-environments-namibia-and-south-africa](http://www.cirdi.ca/project/the-relationship-between-local-procurement-strategies-of-mining-companies-their-regulatory-environments-namibia-and-south-africa).

57 Interview with Diana Kaissy, 12 March 2019.

## Box 2. Examples of local procurement governance challenges

- 1 Local procurement rules in Ghana's mining sector do not differentiate between goods manufactured in Ghana and imported goods resold locally. As a result, while procurement from local companies has increased in recent years, some Ghanaian manufactured goods have been replaced with imported goods.<sup>58</sup> This makes for less value addition and industrial activity, contrary to the government's objective to leverage the mining sector for industrialization.<sup>59</sup>
- 2 One analysis of the implementation of the Nigerian Oil and Gas Industry Content Development Act suggested that a focus on indigenous ownership above other forms of local content reflected an elite-led attempt to consolidate power and wealth.<sup>60</sup>
- 3 SKK Migas, the Indonesian oil and gas regulator, required that Inpex, the operator of the Masela Block, build a floating liquefied natural gas (LNG) facility onshore, against expert advice that warned about cost-efficiency and safety in an earthquake-prone part of the country. Pursuing this floating LNG facility was allegedly due to the influence of politically exposed persons who controlled companies that would benefit from contracts under local content requirements, applicable only onshore.<sup>61</sup>
- 4 The Nigerian Content Development and Monitoring Board (NCDMB) and the Nigerian oil and gas industry's joint qualification system was put in place to monitor supplier awards subject to local procurement requirements. According to one study, this has contributed to improved trust and led to gains in local participation, but concerns persist over the NCDMB's discretion in enforcing local content rules, and tendency to waive the requirement that rights holders meet targets.<sup>62</sup>
- 5 A study on allocation of labor hire and service contracts in mining sites in the Democratic Republic of Congo (DRC) and Ghana showed that many suppliers of temporary labor and other low-value services were connected to traditional leaders, suggesting that companies are using these contracts to secure a license to operate.<sup>63</sup>

See also illustrative corruption case 9 in box 3 below.

- 58 African Center for Economic Transformation, Report on launch of Ghana's National Suppliers' Development Programme (2015), [www.acetforafrica.org/acet/wp-content/uploads/publications/2018/04/NSDP-Launch-Report-2018.pdf](http://www.acetforafrica.org/acet/wp-content/uploads/publications/2018/04/NSDP-Launch-Report-2018.pdf); C. Nyarko and P. Anaman. *An analysis of the economic outcomes of local content regulations: A case study of Ghana's mining industry* (2018). Unpublished working paper.
- 59 The International Institute for Sustainable Development/Intergovernmental Forum on Mining, Minerals, Metals, and Sustainable Development, *Case Study: Ghana: The Importance of Defining Local Procurement* (2018), [www.iisd.org/sites/default/files/publications/case-study-ghana-upstream-linkages.pdf](http://www.iisd.org/sites/default/files/publications/case-study-ghana-upstream-linkages.pdf).
- 60 Jesse Salah Ovidia, "The Nigerian, One Percent, and the Management of National Oil Wealth Through Nigerian Content," *Science & Society*, 77/3 (2013), 338.
- 61 Arnold Sirait. *Anak Usaha Bakrie Incar Proyek Jaringan Pipa Blok Masela* (2016), [katadata.co.id/berita/2016/02/22/anak-usaha-bakrie-incar-proyek-pipa-blok-masela](http://katadata.co.id/berita/2016/02/22/anak-usaha-bakrie-incar-proyek-pipa-blok-masela); Rambu Energy, *SKK Migas expects Inpex to submit revised PoD for Masela block in 2019* (2016), [www.rambuenergy.com/2016/05/skk-migas-expects-inpex-to-submit-revised-pod-for-masela-block-in-2019/](http://www.rambuenergy.com/2016/05/skk-migas-expects-inpex-to-submit-revised-pod-for-masela-block-in-2019/); Inpex. Abadi LNG Project, [www.inpex.co.jp/english/business/indonesia.html](http://www.inpex.co.jp/english/business/indonesia.html).
- 62 Jesse Salah Ovidia. "Local Content and Natural Resource Governance: The Cases of Angola and Nigeria," *The Extractive Industries and Society* (2014), 137-146, [www.researchgate.net/publication/265387964\\_Local\\_content\\_and\\_natural\\_resource\\_governance\\_The\\_cases\\_of\\_Angola\\_and\\_Nigeria](http://www.researchgate.net/publication/265387964_Local_content_and_natural_resource_governance_The_cases_of_Angola_and_Nigeria).
- 63 Sara Geenen. Gold and godfathers: Local content, politics, and capitalism in extractive Industries (World Development, 2019), 6, 123, [www.sciencedirect.com/science/article/abs/pii/S0305750X19301810](http://www.sciencedirect.com/science/article/abs/pii/S0305750X19301810). OECD. Corruption in the extractive value chain: typology of risks, mitigation measures and incentives (2016), 55-56, [www.oecd.org/dev/Corruption-in-the-extractive-value-chain.pdf](http://www.oecd.org/dev/Corruption-in-the-extractive-value-chain.pdf).

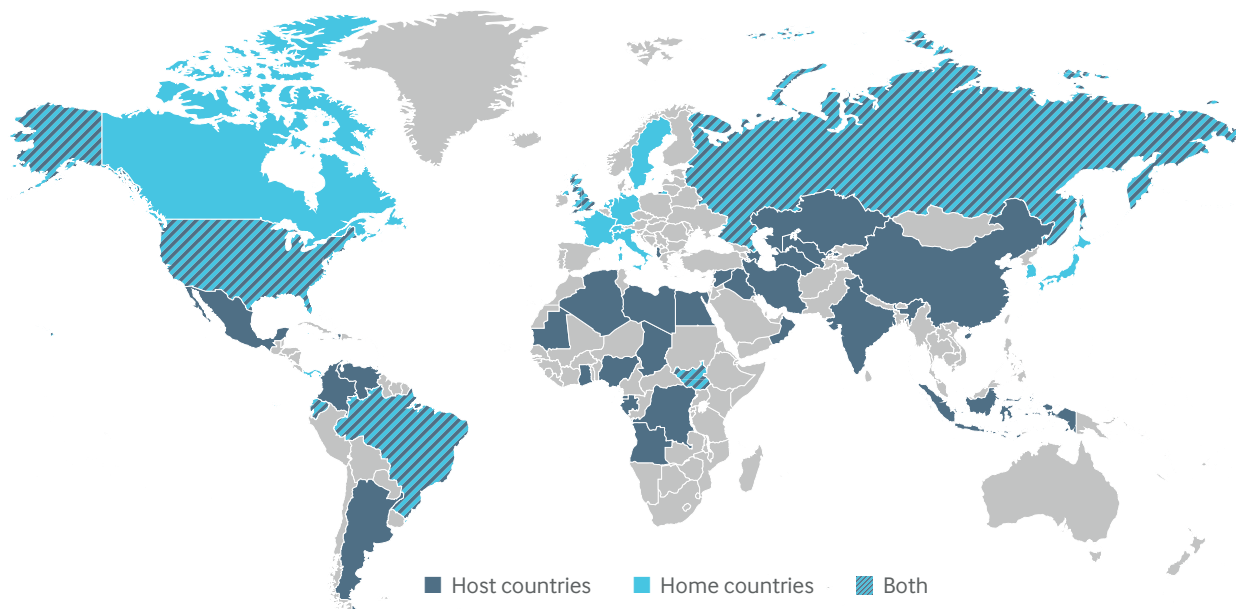


## ISSUE 4. CORRUPTION

**Suppliers have figured in corruption scandals and foreign bribery cases in at least 29 countries across five continents.** (See figure 4.) These numbers are based on our review of over 40 extractive industry supplier corruption cases from around the world, using information from court records, press clippings, academic journals and publicly available databases. Box 3 contains summaries of select cases that illustrate key trends. References to the cases are in parentheses throughout the text.

**The corruption cases feature diverse host countries, companies and goods and services, which suggests that supplier activities are an important node of corruption in both the petroleum and mining sectors.** Supplier corruption has been documented in countries with large extractive sectors and known past corruption challenges such as Nigeria, Kazakhstan, Venezuela and Indonesia. But frontier producers such as Ghana and Mauritania and wealthy economies like the U.S. and the U.K. have also shown signs of vulnerability. The companies implicated have included major international firms headquartered in the U.S., Europe and elsewhere—including rights holders, oilfield service companies, equipment providers, engineering and construction companies and logistics firms—as well as smaller specialized consultants, agents and local suppliers. Host country SOEs also play a role in many cases. As the OECD has flagged, bribery and other misconduct is common at the development phase of extractive projects where there are large capital outlays, but cases occur throughout the project lifecycle.<sup>64</sup>

Figure 4. Selected countries with cases of extractives supplier-related corruption<sup>65</sup>



64 OECD, *Corruption in the extractive value chain: typology of risks, mitigation measures and incentives* (2016), 55-56, [www.oecd.org/dev/Corruption-in-the-extractive-value-chain.pdf](http://www.oecd.org/dev/Corruption-in-the-extractive-value-chain.pdf).

65 Authors' analysis of supplier corruption cases. We sourced cases from the Stanford Law School Foreign Corruption Practices Act Clearinghouse, [fcpa.stanford.edu/index.html](http://fcpa.stanford.edu/index.html); TRACE International Compendium of enforcement actions involving transnational bribery of a government official [www.traceinternational.org/resources-compendium](http://www.traceinternational.org/resources-compendium); the U.K. Serious Fraud Office website [www.sfo.gov.uk/our-cases/](http://www.sfo.gov.uk/our-cases/); The World Bank's Stolen Asset Recovery Initiative (STAR) website, [star.worldbank.org/corruption-cases](http://star.worldbank.org/corruption-cases); and academic literature and media sources.

**Some suppliers offer bribes or illicit financial rewards to gain advantage on particular deals.** They may do this to win or retain contracts, enjoy preferential contract terms, or buy their way out of compliance with regulatory requirements—rules on tax, customs and immigration, or environment, health and safety, for instance. Targets of bribes may include decision makers in the private sector or officials in government agencies or SOEs. Either the bribe maker or bribe taker can initiate the payment. (See cases 1 to 4.)

**In other instances, companies use suppliers to pay bribes or hide channels of influence.** Rights holders or supplier companies may hire a third party, and then route a bribe payment through that actor. This creates some distance between themselves and the ultimate bribe recipient and offers plausible deniability. Some suppliers act as facilitators of corruption in addition to offering other legitimate services, while others appear to exist for the sole purpose of receiving a bribe. (See case 8.) According to the available cases, types of suppliers that carry elevated bribery risks include: those paid on commissions, such as sales agents and distributors; professional service providers that help companies engage with bureaucratic processes, such as freight forwarding companies, customs agents and accountants; and firms that provide services with outputs that are intangible or that are hard to value objectively such as consulting and property rentals. (See cases 4 and 5 to 8.)

**Political elites can also manipulate supplier contracting processes for their own benefit.** Suppliers with strong political support can, in some countries, receive favorable access to award processes, inflated contracts, leniency from regulation or tax liabilities and other advantages. In some contexts, these practices play out in a nuanced and systemic manner, and may be entirely legal. The documented examples we reviewed showed political elites use the following channels to wield influence over supplier contracting processes:

- Influencing the procurement processes used by their SOEs (case 9)
- Allowing or actively pushing for rights holders, large suppliers and SOEs to award inflated supplier contracts (cases 9 and 11)
- Using regulatory approvals or other means to pressure private oil and mining companies to award contracts to certain politically favored suppliers (case 10)
- Participating in the sector by proxy. When companies that are secretly linked to the political figure profit from supplier deals, the political figure may receive a cut of the profits or can direct the proxy to use the funds in certain ways when needed (cases 10 and 12)
- Using supplier contracts for patronage purposes or to drum up political support, such as steering wealth towards certain politically important sub-regions or local powerbrokers (case 9, 11 and 12; see also box 2 on local procurement challenges)

**Economic elites can also use their power and connections to influence government policy and practices for the benefit of their own companies.**

This phenomenon, called “state capture” in its most serious forms, involves private actors exerting undue influence over the formation of the government’s laws, policies and regulations, as well as their implementation.<sup>66</sup> Political financing is one common way that economic elites acquire this kind of influence. Once politicians and public officials are dependent on economic elites for financing, these groups can pressure them to adopt favorable stances. As they strengthen their influence, economic elites may seek to change the very definition of corruption, resulting in situations where many methods of exercising their influence are entirely legal.<sup>67</sup> (See cases 11 to 14.)

**The unique and complex roles that SOEs occupy create high corruption risks.** SOEs are often a locus for supplier bribes and important vehicles through which political and economic elites exert their influence over supplier decision making. Vulnerabilities stem from weak oversight, coupled with broad powers to hire suppliers and influence the procurement decisions of private sector operators. Moreover, their multiple overlapping roles mean that it may be hard to pinpoint their exact modes of influence. As joint venture partners, SOEs may participate in various project committees including those involved in supplier selection and approval, while also playing regulatory roles for the state.<sup>68</sup> (See cases 1 to 3, 5 to 6 and 9 to 12.)

*State-owned enterprises are often a locus for supplier bribes and important vehicles through which political and economic elites exert their influence over supplier decision making.*

**Greater public awareness of the corruption risks around suppliers can help in multiple ways.** First, when there is more scrutiny of corruption risks and the behavior of those involved in governing suppliers, corrupt actors may tread more carefully. Second, scrutiny can reveal problem areas that enable wrongdoing, such as gaps or loopholes in the law, opaque decision-making processes, agencies with limited remits or capacities, or officials with excessive discretionary powers. Third, wider discussion on corruption can add moral support and legitimacy to public oversight actors willing to stand up to narrow interests.

66 Joel Hellman and Daniel Kaufmann. State Capture in Transition, submission to the Judicial Commission of Inquiry into Allegations of State Capture, Corruption and Fraud in the Public Sector including Organs of State (2018), [www.resourcegovernance.org/sites/default/files/documents/state-capture-in-transition.pdf](http://www.resourcegovernance.org/sites/default/files/documents/state-capture-in-transition.pdf).

67 *Ibid.*, 8-12.

68 Delahay and Schmalz, *Why Upstream Oil and Gas Poses Lower Transfer Pricing Risks Than Other Industries*, 181-2.

### Box 3. Illustrative examples of alleged bribery, elite influence, conflicts of interest and political financing involving extractive industry suppliers

**Note:** The examples in this box illustrate some general themes discussed above. Not all of those described led to criminal convictions; some only prompted suspicion, controversy or lesser types of official responses. Others led to legal action, but the cases were later dropped or settled without a guilty plea. We do not suggest that the actors in these cases engaged in any illegal activity—indeed their actions may have been lawful in the relevant jurisdictions. However, all of the cases illustrate the kind of allegations and unfortunate controversy that can arise when supplier behavior shows common warning signs of corruption. Some of the cases mentioned here are subject to active investigations and legal proceedings at the time of publication. We encourage readers of this report to check the status of any of the cases for the most up-to-date and complete information.

#### Supplier pays a bribe to gain advantage on particular deals

- 1 According to U.K. court documents, a company engaged by Rolls Royce paid bribes to Nigerian public officials in order to obtain commercial advantage for Rolls Royce on two supplier tenders between 2009 and 2013. Rolls Royce ultimately withdrew from one tender because the product was unsuitable. It was on course to win the other tender, but withdrew after concerns were raised internally about the receipt of confidential competitor information.<sup>69</sup>
- 2 U.S. court documents show that executives at New Jersey based firm PetroTiger paid USD 333,500 in bribes to an official at EcoPetrol, Colombia's national oil company, to win a service contract worth USD 39.6 million in or around 2009 to 2010.<sup>70</sup>
- 3 The U.S. Securities and Exchange Commission (SEC) alleged that between 2007 and 2010, employees at Saipem, an Italian oilfield services company that was at the time controlled by ENI, paid approximately 198 million EUR to an intermediary to assist in obtaining contracts worth over USD 10 billion from the Algerian national oil company. The intermediary allegedly channeled a portion of that money through offshore shell entities to Algerian officials or their designees.<sup>71</sup> In its settlement agreement with the SEC, ENI agreed to pay a fine of USD 24.5 million and did not admit or deny the charges. In 2020, an Italian court of appeals overturned Saipem's corruption conviction in this matter.
- 4 In 2018, a U.K. court convicted FH Bertling executives of paying over GBP 350,000 in bribes to ConocoPhillips employees to secure a freight forwarding contract worth over GBP16m for the "Jasmine" North Sea oil exploration project and separately to obtain assurance that the inflated prices it charged for additional services would be waved through by ConocoPhillips staff.<sup>72</sup>

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69 Serious Fraud Office versus Rolls Royce PLC, Deferred Prosecution Agreement – Statement of Facts (2017), 32-37, [www.sfo.gov.uk/cases/rolls-royce-plc](http://www.sfo.gov.uk/cases/rolls-royce-plc).

70 United States of America versus Joseph Sigelman, Indictment (2014), 3-4, [www.justice.gov/sites/default/files/criminal-fraud/legacy/2014/05/15/sigelman-indictment.pdf](http://www.justice.gov/sites/default/files/criminal-fraud/legacy/2014/05/15/sigelman-indictment.pdf).

71 Securities and Exchange Commission, In the Matter of Eni S.p.A., Order Instituting Cease and Desist Proceedings (2020), [www.sec.gov/litigation/admin/2020/34-88679.pdf](http://www.sec.gov/litigation/admin/2020/34-88679.pdf); Will Fitzgibbon, Oil Giant Eni To Pay Millions Over 'Sham Contracts' In Panama Papers Bribery Case, (International Consortium of Investigative Journalists, 2020), [www.icij.org/investigations/panama-papers/oil-giant-eni-to-pay-millions-over-sham-contracts-in-panama-papers-bribery-case](http://www.icij.org/investigations/panama-papers/oil-giant-eni-to-pay-millions-over-sham-contracts-in-panama-papers-bribery-case).

72 U.K. Serious Fraud Office, "9 convicted in £16m and \$21m FH Bertling bribery cases" (2018), [www.sfo.gov.uk/2018/11/27/9-convicted-in-16m-and-21m-fh-bertling-bribery-cases](http://www.sfo.gov.uk/2018/11/27/9-convicted-in-16m-and-21m-fh-bertling-bribery-cases).

#### Use of suppliers to pay bribes or hide channels of influence

- 5 In March 2019, two former heads of Unaoil, a Monaco-based company, pled guilty to U.S. charges for their roles in facilitating millions of dollars in bribes to officials in multiple countries in order to help Unaoil's clients secure oil and gas supply contracts.<sup>73</sup> As many as 11 oilfield services and construction companies that were Unaoil clients have faced related legal proceedings.<sup>74</sup>
- 6 In one Unaoil-related case, U.S. court documents state that SBM Offshore made corrupt "commission" payments to sales agents around the world between 1996 and 2012, knowing that a portion of these payments would be used to bribe foreign officials in Brazil, Angola, Equatorial Guinea, Kazakhstan, Iraq and elsewhere.<sup>75</sup>
- 7 Between 2010 and 2014, according to U.S. SEC findings, rights holder Kinross Mining hired and made payments to consultants connected with Ghanaian government officials to expedite processing of visas and permits, receive environmental authorizations and process customs documents.<sup>76</sup>
- 8 A Canadian court found that Griffiths Energy used a supplier company to bribe Chadian diplomats in 2009. Griffiths entered into an agreement with a front company set up by the diplomats, and promised to pay a "consulting fee" of USD 2 million as well as discounted shares if it succeeded in securing the development rights to two oil blocks in Chad. The wife of the Chadian ambassador to the U.S. and Canada was the front company's sole officer, director and shareholder.<sup>77</sup>

#### Elite influence, conflicts of interest and political financing

- 9 In the wake of Brazil's "Lava Jato" scandal, court filings, NGO reports and investigative journalism has described how politicians, political parties and construction company magnates enjoyed high levels of inappropriate influence over the national oil company Petrobras, and its procurement systems. To route resource rents into private hands, these players systematically altered procurement rules, inflated contract values and constrained competition.<sup>78</sup> In one variation, construction companies formed a cartel to bid for Petrobras contracts, with Petrobras officials offering advice on how high the companies could bid.<sup>79</sup> In a number of instances, Petrobras officials would pick winners and other members of the cartel would submit uncompetitive bids knowing they would have priority in future contracts.<sup>80</sup> A large number of politicians and Petrobras officials received kickbacks from the scheme, which generated as much as USD5 billion in bribes.<sup>81</sup>

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73 U.S. DOJ, Oil Executives Plead Guilty for Roles in Bribery Scheme Involving Foreign Officials (2019), [www.justice.gov/opa/pr/oil-executives-plead-guilty-roles-bribery-scheme-involving-foreign-officials](http://www.justice.gov/opa/pr/oil-executives-plead-guilty-roles-bribery-scheme-involving-foreign-officials).

74 Galizia, *Greasing the wheels*.

75 United States of America versus SBM Offshore N.V., Deferred Prosecution Agreement, Statement of Facts (2017), 7-9, [www.justice.gov/opa/press-release/file/1014801/download](http://www.justice.gov/opa/press-release/file/1014801/download).

76 Securities and Exchange Commission, In the Matter of Kinross Gold Corporation, Administrative Order Instituting Cease and Desist Proceedings (2017), 3-5, [www.sec.gov/litigation/admin/2018/34-82946.pdf](http://www.sec.gov/litigation/admin/2018/34-82946.pdf).

77 Tyler Hodgson and Nicolas Businger. Griffiths Energy International pleads guilty to CFPOA charges; FCPA investigation outstanding. (Lexology, 2013), [www.lexology.com/library/detail.aspx?g=a8bdcc80-f942-45a3-939c-6db694571f4a](http://www.lexology.com/library/detail.aspx?g=a8bdcc80-f942-45a3-939c-6db694571f4a); The Serious Fraud Office versus Saleh, EWHC 2119, (High Court of Justice Queen's Bench Division, 2015), [www.bailii.org/ew/cases/EWHC/QB/2015/2119.html](http://www.bailii.org/ew/cases/EWHC/QB/2015/2119.html).

78 In 1998, for example, the government passed decree 2.745/98 so that Petrobras did not have to comply the government procurement law. Natália Rezende de Almeida Santos. Internal Controls and Corruption: The case of Petrobras (2017), 22, [pingpdf.com/pdf-internal-controls-and-corruption-university-of-sussex.html](http://pingpdf.com/pdf-internal-controls-and-corruption-university-of-sussex.html).

79 United States of America versus Odebrecht S.A., Plea Agreement, (2016), p.B-12-B14, [www.justice.gov/opa/press-release/file/919916/download](http://www.justice.gov/opa/press-release/file/919916/download), p. B-12.

80 United States Southern District of New York, in re: Petrobras Securities Litigation, Consolidated Second Amended Class Action Complaint, 16 Jul 2015, p. 23 & 102, [securities.stanford.edu/filings-documents/1053/PBSP00\\_01/2015716\\_r01c\\_14CV09662.pdf](http://securities.stanford.edu/filings-documents/1053/PBSP00_01/2015716_r01c_14CV09662.pdf); U.S. DOJ, *Petroleo Brasileiro S.A.—Petrobras, Non-prosecution agreement*, p. A-6, [www.justice.gov/opa/press-release/file/1096706/download](http://www.justice.gov/opa/press-release/file/1096706/download).

81 Antônio Sampaio, "Forget its ousted politicians. Here's the real cost of Brazil's corruption," *Washington Post*, 24 August 2017, [www.washingtonpost.com/news/democracy-post/wp/2017/08/24/forget-its-ousted-politicians-heres-the-real-cost-of-brazils-corruption](http://www.washingtonpost.com/news/democracy-post/wp/2017/08/24/forget-its-ousted-politicians-heres-the-real-cost-of-brazils-corruption).



- 10 U.S. SEC records from 2017 describe how Halliburton personnel, under pressure from Angolan government insiders, signed a contract with a politically connected supplier in order to meet the country's local content rules. The local Angolan company was owned by a former Halliburton employee and a friend and neighbor of an official at the national oil company Sonangol who had authority to veto or reduce subcontracts awarded to Halliburton. Halliburton ultimately paid the company USD 3.7 million for services that the company mostly did not provide.<sup>82</sup>
- 11 In recent years, a number of analysts and investigative journalists have alleged that the Russian SOEs Rosneft and Gazprom allocate lucrative supplier contracts in ways that consolidate wealth in the hands of well-connected economic elites.<sup>83</sup> In turn, the reports argue, these projects helped fuel the rise of several billionaire oligarchs with close ties to Russian political leadership.<sup>84</sup> As one example of the potential costs of this alleged behavior, industry observers have estimated that some Gazprom-constructed pipelines cost three times the standard industry costs.<sup>85</sup>
- 12 Investigations conducted by two international NGOs in 2018 alleged that in South Sudan, political leaders used the national oil company, Nile Petroleum Corporation, to procure military equipment from suppliers with ties to government officials. The NGOs claimed that this formed part of a wider pattern of the SOE funding militia activity in South Sudan's ongoing civil conflict.<sup>86</sup>
- 13 In 2011, two former Alaska legislators pled guilty to political corruption and were sentenced in federal court after an oilfield service company, VECO Corporation, paid bribes to push for legislative measures from which it would profit. These included a version of an oil tax bill the company had drafted and legislation that would lead to the construction of a new gas pipeline.<sup>87</sup>
- 14 Some efforts by suppliers to impact public policy are legal but nevertheless show how they seek to acquire special influence over government decision makers. In the U.S., Halliburton works hard to influence policy and maintain ties with politicians. In 2018, it spent half a million dollars to support candidates running for office. A watchdog group found that several Halliburton lobbyists also previously held government jobs and at least six members of the U.S. Congress held shares in the company.<sup>88</sup>

82 Securities and Exchange Commission, In the Matter of Halliburton Company and Jeannot Lorenz, Administrative Order Instituting Cease and Desist Proceedings (2017), 6, [www.sec.gov/litigation/admin/2017/34-81222.pdf](http://www.sec.gov/litigation/admin/2017/34-81222.pdf).

83 Alexandra Gillies. *Crude Intentions*, 124-5.

84 Karen Dawisha. *Putin's Kleptocracy* (2015), 92-93; U.S. Treasury Department, Treasury Sanctions Russian Officials, Members Of The Russian Leadership's Inner Circle, And An Entity For Involvement In The Situation In Ukraine (2014), [www.treasury.gov/press-center/press-releases/Pages/jl23331.aspx](http://www.treasury.gov/press-center/press-releases/Pages/jl23331.aspx); Joshua Yaffa, "Putin's Shadow Cabinet and the Bridge to Crimea," *The New Yorker*, 29 May 2017, [www.newyorker.com/magazine/2017/05/29/putins-shadow-cabinet-and-the-bridge-to-crimea](http://www.newyorker.com/magazine/2017/05/29/putins-shadow-cabinet-and-the-bridge-to-crimea).

85 *Ibid.*

86 Global Witness, *Capture on the Nile* (2018), [www.globalwitness.org/en/campaigns/south-sudan/capture-on-the-nile](http://www.globalwitness.org/en/campaigns/south-sudan/capture-on-the-nile); The Sentry, *Fueling Atrocities: Oil and War in South Sudan*, (2018), 2, [www.thesentry.org/reports/fueling-atrocities](http://www.thesentry.org/reports/fueling-atrocities).

87 Federal Bureau of Investigation, "Former Alaska Legislators Peter Kott and Victor Kohring Convicted and Sentenced for Public Corruption Crimes" (2011), [archives.fbi.gov/archives/anchorage/press-releases/2011/former-alaska-legislators-peter-kott-and-victor-kohring-convicted-and-sentenced-for-public-corruption-crimes](http://archives.fbi.gov/archives/anchorage/press-releases/2011/former-alaska-legislators-peter-kott-and-victor-kohring-convicted-and-sentenced-for-public-corruption-crimes).

88 OpenSecrets.org, Halliburton Co, Profile for the 2018 Election Cycle, [www.opensecrets.org/orgs//summary?id=D000000281](http://www.opensecrets.org/orgs//summary?id=D000000281).

## Toward supplier transparency: Building on existing practice

**A general lack of awareness and accountability about the role extractive industry suppliers play is standing in the way of effective oversight.** This presents challenges for government officials charged with developing policy and regulating the industry; local business communities seeking to engage with project supply chains; and public oversight actors such as journalists or civil society advocates seeking to ensure that oil, gas and mining bring benefits to citizens.

**Transparency is a necessary first step to improving awareness, engagement and accountability.** We are still a long way away from what is needed, however some stakeholders are already publishing useful information about extractive industry suppliers and many global reporting and transparency standards are incorporating supplier disclosures into their requirements and guidelines. (See annex 1.) In what follows, we document existing disclosure practices spanning four key areas of supplier management: procurement processes, supplier identities, spending on suppliers and supplier taxation. For each, we outline what is being done, why the information is useful, and what potential gaps or challenges surround the current approaches to disclosure. (See annex 2 for examples.) Finally, in box 4, we show how publicly available information on suppliers has been used to improve oversight.

*We are still a long way away from what is needed, however some stakeholders are already publishing useful information about extractive industry suppliers.*

### PROCUREMENT PROCESS

**Disclosure of the rules that govern procurement and communication around specific processes of procurement could deliver accountability benefits.**

Rights holders and suppliers could mitigate supply chain risks and gain greater public trust by showing that their working relationships are the result of open and fair processes. Local businesses could build better awareness of procurement opportunities and how to apply for them. Governments and public oversight actors could scrutinize supplier selection processes, especially those of SOEs, reducing the risk of mismanagement and corruption.

- **Rights holders.** In line with sustainability reporting guidelines such as the Global Reporting Initiative (GRI), most large, international rights holders provide general company-wide information about the rules that govern procurement, including basic information about approaches to due diligence.<sup>89</sup> Many companies also publish supplier policies and statements, including code of conduct documents.<sup>90</sup> However, comparatively fewer companies publish practical procurement information at the project level. One important exception is the Rio Tinto-operated Oyu Tolgoi mine in Mongolia, which

<sup>89</sup> See, for example, Exxon Mobil [corporate.exxonmobil.com/Community-engagement/Sustainability-Report/Social/Supply-chain-management#procurementProcessAndSupplierQualification](http://corporate.exxonmobil.com/Community-engagement/Sustainability-Report/Social/Supply-chain-management#procurementProcessAndSupplierQualification); Shell, [www.shell.com/business-customers/shell-for-suppliers/about-shell-for-suppliers.html](http://www.shell.com/business-customers/shell-for-suppliers/about-shell-for-suppliers.html) and Anglo American, [brasil.angloamerican.com/~media/Files/A/Anglo-American-Group/Brazil/sustentabilidade/aa-sustainability-report-2018.pdf](http://brasil.angloamerican.com/~media/Files/A/Anglo-American-Group/Brazil/sustentabilidade/aa-sustainability-report-2018.pdf).

<sup>90</sup> See, for example, Rio Tinto, [www.riotinto.com/footer/suppliers](http://www.riotinto.com/footer/suppliers); and Equinor, [www.equinor.com/en/supply-chain.html#downloads](http://www.equinor.com/en/supply-chain.html#downloads).

publishes detailed project-level information about procurement policies, procedures and standards, as well as practical information about upcoming tenders and expressions of interest and how to apply.<sup>91</sup>

- **SOEs.** Because SOEs are public institutions, their procurement rules may be included in laws or public policy documents. Nevertheless, many SOE procurement procedures are complex and poorly communicated. EcoPetrol has made an effort to provide company-level information in line with sustainability reporting guidelines on procurement.<sup>92</sup> Other SOEs, including Pemex, Petrobras and Qatar Petroleum have developed procurement portals that provide detailed information about specific processes, upcoming tenders and contracts awarded.<sup>93</sup> A novel approach to procurement transparency exists in Mexico, where the general contracting provisions of Pemex also allow for “social witnesses” to participate in the various stages of the SOE’s procurement processes. “Social witnesses” are individuals that witness the different procurement stages and are expected to publish their observations, recommendations and report on irregularities.<sup>94</sup> While these provisions allow for unrivaled public access to procurement decision making, the highly complex and technical nature of SOE procurement sometimes means that social witnesses are not always able to effectively detect irregularities.<sup>95</sup>
- **Host governments.** Some governments have established platforms for companies to transparently share procurement information and business opportunities. The U.K. Oil and Gas Authority, for example, encourages rights holders to publish award details on the Oil and Gas Pathfinder portal. In addition to basic contextual information, the portal allows companies to list the main contracts they have awarded, the value bracket of those contracts and who users can contact for further information.<sup>96</sup> Other countries have pursued more legalistic approaches. In Mexico, for example, the rights holder must issue an invitation for a contest or public international bidding process for contracts of value greater than USD20 million.<sup>97</sup> Meanwhile, the law in Lebanon requires companies to undertake open bidding for major contracts.<sup>98</sup>

91 Oyu Tolgoi, *Procurement*, [www.ot.mn/oyu-tolgoi-procurement](http://www.ot.mn/oyu-tolgoi-procurement).

92 Ecopetrol, Sustainability Report (2018), 191-199, [www.ecopetrol.com.co/documentos/Ecopetrol-Integrated-Sustainability-Report-2018.pdf](http://www.ecopetrol.com.co/documentos/Ecopetrol-Integrated-Sustainability-Report-2018.pdf).

93 Petrobras, Portal de Transparência, [transparencia.petrobras.com.br/licitacoes-contratos/contratos](http://transparencia.petrobras.com.br/licitacoes-contratos/contratos); Pemex, Portal de Obligaciones de Transparencia, [portaltransparencia.gob.mx/pot/contrataciones/consultarContrato.do?method=consultaContrato&id.idContrato=645018814&\\_idDependencia=18575&viaLocation=true](http://portaltransparencia.gob.mx/pot/contrataciones/consultarContrato.do?method=consultaContrato&id.idContrato=645018814&_idDependencia=18575&viaLocation=true); Qatar Petroleum, Tenders, [qp.com.qa/en/SupplyManagement/Tenders/Pages/Tenders.aspx](http://qp.com.qa/en/SupplyManagement/Tenders/Pages/Tenders.aspx). Accessed July 2020.

94 C.A. Morán and A. Carvallo, “Pemex’s Contracting Regime After the Energy Reform” (Oil, Gas, and Energy Law, 2016), [www.ogel.org/article.asp?key=3602](http://www.ogel.org/article.asp?key=3602).

95 Interview with Gavin Hayman, 15 May 2019.

96 Oil and Gas Authority, Oil and Gas Pathfinder, [www.ogauthority.co.uk/supply-chain/oil-gas-pathfinder-previously-project-pathfinder](http://www.ogauthority.co.uk/supply-chain/oil-gas-pathfinder-previously-project-pathfinder).

97 Comisión Nacional de Hidrocarburos, *Rondas Mexico*, [rondasmexico.gob.mx](http://rondasmexico.gob.mx)

98 These are defined as “any contract that materially or substantially affects the design or functionality of Facilities, the concept or timeline of Development, Production or resource management and depletion policies. ... contracts of substantial value, meaning that the performance or non-performance of the contract may substantially affect the economy of the project or the financial strength of the Right Holder.” Government of Lebanon, Petroleum Activities Regulations, Article 157.

One important challenge relating to the disclosure of procurement rules and processes centers around the level at which SOEs, rights holders and governments make disclosures. Communicating general procurement rules and processes at the company level is slowly emerging as common practice. However, at the level of individual projects, where information is more useful and public demand is greatest, procurement information tends to be more limited. If stakeholders want to gain the benefits of transparency, it will be necessary to match required disclosures with information needs and demands.

*If stakeholders want to gain the benefits of transparency, it will be necessary to match required disclosures with information needs and demands.*

## SUPPLIER IDENTITIES

**Publication of supplier identities enables government officials, rights holders and oversight actors to identify suppliers that may pose challenges for the country's taxation, local content or anti-corruption efforts.** Moreover, they can more effectively detect potential conflicts of interest when information on supplier identities is combined with information on beneficial ownership.<sup>99</sup> Transparency of supplier identities also helps local businesses gain awareness of which supplier companies may have further contracting opportunities available.

- **Rights holders.** The operators of the Oyu Tolgoi mine in Mongolia maintain an updated list of suppliers awarded contracts on the company's procurement website. Each supplier has a listed contact person with contact information and website details.<sup>100</sup> For key contracts on the U.K. continental shelf, several petroleum companies including Alpha Petroleum, BP, Dana Petroleum, Neptune E&P and Total have published project-level information including supplier names and points of contact using the U.K. Oil and Gas Authority Oil and Gas Pathfinder portal.
- **SOEs.** Some SOE contract portals allow users to search and browse through lists of SOE contract recipients. Petrobras' transparency portal provides information on the contractor name, contract objective, the contract value and the gross balance of the contract.<sup>101</sup> Pemex's and Qatar Petroleum's portals provide this information, plus information on the specific type of recruitment process (open tender, invitation to bid, etc.) under which it selected the supplier.<sup>102</sup>
- **Host governments.** The U.K. Oil and Gas Authority Oil and Gas Pathfinder portal allows companies to list the main contracts they have awarded, including the identity of the winning company and who can be contacted for further information.<sup>103</sup> Nigeria's Content Development and Monitoring Board publishes the identities of approved suppliers.<sup>104</sup> In Lebanon, the oil

99 A beneficial owner is a natural person who, directly or indirectly, exercises substantial control over, has a substantial economic interest in, or receives substantial economic benefit from a corporate entity. Increasingly countries around the world are collecting—and in some cases, publishing—beneficial ownership information in public registers. Where supplier identities are published, availability of beneficial ownership information would allow governments, the private sector and oversight actors to better prevent, monitor and manage problematic supplier relationships where they arise. Erica Westenberg and Aaron Sayne. "Beneficial Ownership Screening: Practical Measures to Reduce Corruption Risks in Extractives Licensing" (NRGI, 2018), 11, [www.resourcegovernance.org/sites/default/files/documents/beneficial-ownership-screening\\_0.pdf](http://www.resourcegovernance.org/sites/default/files/documents/beneficial-ownership-screening_0.pdf).

100 Oyu Tolgoi, "Oyu Tolgoi underground awarded contract listing," [www.ot.mn/oyu-tolgoi-underground-awarded-contract-listing](http://www.ot.mn/oyu-tolgoi-underground-awarded-contract-listing).

101 Petrobras, Portal de Transparência.

102 Pemex, Portal de Obligaciones de Transparencia; Qatar Petroleum, Tenders.

103 Oil and Gas Authority, Oil and Gas Pathfinder.

104 Nigerian Content Development and Monitoring Board, Approved suppliers list 2018/2019, [ncdmb.gov.ng/ease-of-doing-business/ncec-approved-list](http://ncdmb.gov.ng/ease-of-doing-business/ncec-approved-list).

sector transparency law requires publication of the names of all suppliers in the industry.<sup>105</sup> Cameroon's mining code goes one step further and requires direct sub-contractors of mining license holders and applicants to disclose their beneficial owners.<sup>106</sup> Some countries, such as Guinea and Iraq, have provided information on the ownership structures of suppliers in their EITI reporting.<sup>107</sup>

The publication of supplier identities faces two core challenges. First is the choice of reporting thresholds. Publishing information on every small, low-value supplier involved in a project or sector may risk overwhelming the user and burying important information. Conversely, high thresholds could leave out small but locally-important companies through which political elites exercise influence and receive benefits. Second is the issue of commercial sensitivity. Some rights-holding companies have asserted that information on supplier identities is commercially sensitive and so should not be published.<sup>108</sup> These concerns merit further examination. But, as we identify above, several rights-holding companies have already disclosed this information for multiple projects. Moreover, multinational companies in other sectors have already embraced comprehensive disclosure of supplier identities. In the garment industry, for example, at least 39 leading global brands have signed on to the Transparency Pledge, under which they have committed to publish global factory lists with detailed information about suppliers, subcontractors and licensees.<sup>109</sup>

## RIGHTS HOLDER SPENDING ON SUPPLIERS

### **Better oversight of supplier cost controls, taxation, local procurement and corruption risks all depend on information about spending on suppliers.**

Transparency can help governments and citizens understand the scale and composition of spending on suppliers and help rights holders to communicate the broader economic impacts of their operations. It can also make spending by SOEs more accountable.

- **Rights holders.** A common approach carried out by a range of companies is the publication of the total number of suppliers worldwide and the total amount spent on them.<sup>110</sup> Several companies go further. BHP, Anglo American and

105 Government of Lebanon Law 84 Issued on the 10th of October: Enhancing Transparency in the Petroleum Sector, Article 10.7, [www.lpa.gov.lb/Library/Assets/Gallery/asdasdas/Laws/Transparency%20Law%20-%20English%20-%20Unofficial%20Translation%20-%20law%2084-2018.pdf](http://www.lpa.gov.lb/Library/Assets/Gallery/asdasdas/Laws/Transparency%20Law%20-%20English%20-%20Unofficial%20Translation%20-%20law%2084-2018.pdf).

106 République du Cameroun, Loi N°2016/017 du 14 Décembre 2016 Code Minier, Article 145, [www.droit-afrique.com/uploads/Cameroun-Code-minier-2016.pdf](http://www.droit-afrique.com/uploads/Cameroun-Code-minier-2016.pdf).

107 Toroskainen and Lado, *EITI Data Can Support Guinea's Efforts to Promote Local Mining Subcontractors; EITI, Spotlight: Transparency in the supply of goods and services in the extractive industries* (2020), Implementation Progress Report October – January 2020, Board paper 46-2-A.

108 Interview with Jeff Geipel, 12 October 2019.

109 Examples include, but are not limited to Adidas, [www.adidas-group.com/en/sustainability/managing-sustainability/human-rights/supply-chain-structure/](http://www.adidas-group.com/en/sustainability/managing-sustainability/human-rights/supply-chain-structure/), Nike, [manufacturingmap.nikeinc.com/](http://manufacturingmap.nikeinc.com/); and Primark, [globalsourcingmap.primark.com/](http://globalsourcingmap.primark.com/). See Human Rights Watch, "Surge in Garment Industry Transparency" (2019), [www.hrw.org/news/2019/12/18/surge-garment-industry-transparency](http://www.hrw.org/news/2019/12/18/surge-garment-industry-transparency).

110 See, for example, BP, *Sustainability report* (2018), 42, [www.bp.com/content/dam/bp/business-sites/en/global/corporate/pdfs/sustainability/group-reports/bp-sustainability-report-2018.pdf](http://www.bp.com/content/dam/bp/business-sites/en/global/corporate/pdfs/sustainability/group-reports/bp-sustainability-report-2018.pdf); Rio Tinto, *Taxes paid report* (2018), [www.riotinto.com/en/news/releases/Rio-Tinto-taxes-paid-report-2018](http://www.riotinto.com/en/news/releases/Rio-Tinto-taxes-paid-report-2018); Shell, *Contribution to society* (2018) 77, [reports.shell.com/sustainability-report/2018/contribution-to-society.html](http://reports.shell.com/sustainability-report/2018/contribution-to-society.html) - :":text=Our contribution to society comes,through our social investment programmes; Total (2018), *Registration document*, 108, [www.total.com/sites/g/files/nytnzq111/files/atoms/files/ddr2018-en.pdf](http://www.total.com/sites/g/files/nytnzq111/files/atoms/files/ddr2018-en.pdf) - page=382.



Tullow Oil are among a group of companies that disaggregate their spending on suppliers by country, with the latter two further breaking out local supplier spending.<sup>111</sup> Project-level reporting is more common in the mining sector. Examples include Ivanhoe mines and Lundin Gold (both using the Mining Local Procurement Reporting Mechanism (LPRM)), AngloGold Ashanti operated Geita Mine in Tanzania, and Oyu Tolgoi in Mongolia, which has published detailed procurement spend targets against actual figures for 2017.<sup>112</sup>

- **SOEs.** Information on SOE expenditures is generally poor: one of the key findings of NRCI's National Oil Company Database project has been that company expenditures remain a major gap in SOE reporting.<sup>113</sup> Yet, examples of good practice do exist. Thai national oil company, PTT Exploration and Production Public Company Limited, provides information on total spending on suppliers across four countries where it works and publishes the percentage of local procurement in five countries. For spending in Thailand, it disaggregates supplier numbers and total spend figures across industry segments.<sup>114</sup> Colombian national oil company EcoPetrol publishes figures on its contracting in Colombia including the total number of suppliers, the total spend on suppliers and disaggregated figures for spending on local suppliers.<sup>115</sup> Brazilian national oil company Petrobras discloses information on spending on suppliers for its subsidiaries. It gives broad figures about how many suppliers are based in Brazil and further disaggregates suppliers by size of contract.<sup>116</sup> Qatar Petroleum publishes tender opportunities and information about awarded contracts, agreements and purchase orders on its website, including name of supplier, contract value and scheduled duration of works.<sup>117</sup>
- **Host governments.** A few governments have developed systems to standardize reporting on spending on suppliers. In many instances, these exist to track local content. The Mexican Hydrocarbons Commission, which publishes project-level procurement spend targets and actual figures for each contract that it manages, is one prominent example.<sup>118</sup> Other countries publish figures in their EITI reports. Senegal's 2018 EITI report, for example, includes the total number of domestic and international suppliers and total value of payments.<sup>119</sup>

111 BHP, *Economic contribution report* (2018) 4, [www.bhp.com/-/media/documents/investors/annual-reports/2018/bhpeconomiccontributionreport2018.pdf](http://www.bhp.com/-/media/documents/investors/annual-reports/2018/bhpeconomiccontributionreport2018.pdf); Anglo American, *Sustainability Report* (2018), 3, [brasil.angloamerican.com/~/\\_/media/Files/A/Anglo-American-Group/Brazil/sustentabilidade/aa-sustainability-report-2018.pdf](http://brasil.angloamerican.com/~/_/media/Files/A/Anglo-American-Group/Brazil/sustentabilidade/aa-sustainability-report-2018.pdf); Tullow Oil, *Annual report and accounts* (2018), 179, [www.tulloil.com/application/files/4115/7960/2840/tullow-oil-plc-2018-annual-report-and-accounts.pdf](http://www.tulloil.com/application/files/4115/7960/2840/tullow-oil-plc-2018-annual-report-and-accounts.pdf).

112 Ivanhoe mines, *Sustainability Report 2018* (2018), 30, [www.ivanhoemines.com/site/assets/files/4354/ivanhoemines\\_sr18.pdf](http://www.ivanhoemines.com/site/assets/files/4354/ivanhoemines_sr18.pdf); Lundin Gold, *Sustainability Report 2019*, 15, [www.lundin.gold.com/site/assets/files/16806/2019-sustainability-report-en.pdf](http://www.lundin.gold.com/site/assets/files/16806/2019-sustainability-report-en.pdf); Geita Mine, *How we have shared gold sales revenue*, [www.geitamine.com/en.html-tax](http://www.geitamine.com/en.html-tax); Oyu Tolgoi, *Procurement in numbers*, [www.ot.mn/procurement/procurement-in-numbers](http://www.ot.mn/procurement/procurement-in-numbers).

113 NRCI, *The National Oil Company Database* (2019), 22, [www.nationaloilcompanydata.org/api/publications/content/NFlnSnhdYNC4ntCohaYqok1u2jHAG4vvLXK1jwrL.pdf](http://www.nationaloilcompanydata.org/api/publications/content/NFlnSnhdYNC4ntCohaYqok1u2jHAG4vvLXK1jwrL.pdf).

114 PTTEP, *Sustainability report* (2018), 48-50, [www.pttep.com/en/Sustainabledevelopment/Disclosure/Sustainabilityreport/2018Sdreport.aspx](http://www.pttep.com/en/Sustainabledevelopment/Disclosure/Sustainabilityreport/2018Sdreport.aspx).

115 Ecopetrol, *Sustainability Report* (2018), 198-199, [www.ecopetrol.com.co/wps/portal/Home/es/!ut/p/z1/04\\_Sj9CPykssy0xPLMnMz0vMAfIjo8zi\\_YzMnA09TQwDDMxCXQwCXV0tAoN8fAzdDUz1wwkpiAJG-AAjgZA\\_VFYIDgaOAUZORkbGLj7G2FVgGJGQW6EQaajoilAyi524w!!/dz/d5/L2dBISevZ0FBIS9nQSEh](http://www.ecopetrol.com.co/wps/portal/Home/es/!ut/p/z1/04_Sj9CPykssy0xPLMnMz0vMAfIjo8zi_YzMnA09TQwDDMxCXQwCXV0tAoN8fAzdDUz1wwkpiAJG-AAjgZA_VFYIDgaOAUZORkbGLj7G2FVgGJGQW6EQaajoilAyi524w!!/dz/d5/L2dBISevZ0FBIS9nQSEh).

116 Petrobras, *Sustainability* (2018), 78-79.

117 Qatar Petroleum, *Tenders*.

118 Comisión Nacional de Hidrocarburos, *Rondas Mexico*, [rondasmexico.gob.mx/eng/contracts/cnh-r01-101-a22015/?tab=08](http://rondasmexico.gob.mx/eng/contracts/cnh-r01-101-a22015/?tab=08).

119 Government of Senegal, *EITI report for 2018* (2019), 110-111, [eiti.org/document/2018-senegal-eiti-report](http://eiti.org/document/2018-senegal-eiti-report).

Though there is strong precedent for publishing information on spending on suppliers, current practice reveals standardization challenges. A significant challenge is the definitions and units of reporting—for example, “spending on suppliers,” “procurement spending” or “local.” Until there is common language, oversight actors will only be able to scrutinize information on a project or company basis, while comparisons across companies or countries will not be possible.

*A significant challenge is the definitions and units of reporting.*

## SUPPLIER TAXATION

**Unlike the disclosure of rights holder tax payments, transparency in the taxation of extractive industry suppliers has not advanced much in recent years.** Publishing more information on how governments tax suppliers would help rights holder and supplier companies better show the economic contribution they make to the countries in which they work and inform debates around optimal tax policies. Progress here may also help ensure that governments do not miss revenue opportunities and highlight bad policy decisions so that lawmakers can correct them.

- **Rights holders and SOEs.** Although the EITI Standard does not require countries to report on withholding taxes paid by rights holders on behalf of their suppliers, some EITI processes, such as in Zambia and the DRC include these in their reporting.<sup>120</sup> Elsewhere, some companies such as Glencore include withholding taxes as part of their payments-to-governments reporting mandated by home governments.<sup>121</sup>
- **Suppliers.** The OECD’s base erosion and profit shifting (BEPS) framework requires multinational companies with consolidated group revenue of at least EUR 750 million to share tax information covering the jurisdictions in which they operate. Under BEPS Action Plan 13, large multinationals must prepare a country-by-country-report with aggregate data on income, profit, income taxes paid and economic activity. Most governments do not require these reports to be made public, but some companies have voluntarily published their country-by-country-reports, and Norway has made publication mandatory in the extractive industries. As result Norwegian service companies such as Aker Solutions have made these reports public.<sup>122,123</sup> Some suppliers are also beginning to proactively publish information about their approach to taxation. For example, Halliburton publishes its tax strategy on its website.<sup>124</sup> Within EITI, extractive industry suppliers are reporting tax payments to governments

<sup>120</sup> Government of Zambia, *EITI report for the year ended 31 December 2017* (2018), 75, [eiti.org/files/documents/2017\\_zambia\\_eiti\\_report.pdf](http://eiti.org/files/documents/2017_zambia_eiti_report.pdf); Government of DRC, *ITIE rapport de conciliation 2017* (2019), 37, [eiti.org/files/documents/rapport\\_de\\_conciliation\\_itie-rdc\\_2017\\_-\\_final\\_signe.pdf](http://eiti.org/files/documents/rapport_de_conciliation_itie-rdc_2017_-_final_signe.pdf).

<sup>121</sup> Glencore, *Payments to governments report, 2018* (2019), 9, 36, [www.glencore.com/dam:jcr/c9cea7dd-9fe6-4f9b-bd6a-e82f72672075/Glencore\\_Payments\\_to\\_governments\\_report\\_2018--.pdf](http://www.glencore.com/dam:jcr/c9cea7dd-9fe6-4f9b-bd6a-e82f72672075/Glencore_Payments_to_governments_report_2018--.pdf)

<sup>122</sup> While no extractive industry supplier companies have voluntarily published country-by-country-reports, some rights-holding companies including ENI, Shell and Anglo American have opted to make reports public. Publication provides companies the opportunity to build public trust in their tax strategy and to add narrative explaining country-by-country-reports.

<sup>123</sup> Aker Solutions, *Corporate Responsibility Report 2018* (2019), 38, [www.akersolutions.com/globalassets/cr/cr-report-2018.pdf](http://www.akersolutions.com/globalassets/cr/cr-report-2018.pdf).

<sup>124</sup> Halliburton, *Halliburton tax strategy* (2019), [www.halliburton.com/en-US/about-us/halliburton-uk-tax-strategy.html?node-id=hgeyxt6e](http://www.halliburton.com/en-US/about-us/halliburton-uk-tax-strategy.html?node-id=hgeyxt6e).

in Guinea, Mali and Tanzania. For example, Mali's 2016 EITI report covers payments to the government from suppliers that amount to 17 percent of total extractive industry revenues, a list of local suppliers, their tax identification numbers, the value of goods and services procured in the reporting period and the nature of goods/services and locality.<sup>125</sup>

- **Host governments.** In addition to including supplier taxation in EITI reporting, many host governments are now publishing resource contracts between the rights holder and the state which often include previously hidden supplier tax exemptions. At least 46 governments have now published state-investor contracts, and 28 have laws in place requiring this publication.<sup>126</sup> Future analysis could examine these contracts for relevant exemptions, building on important initial efforts from the Intergovernmental Forum on Mining, Minerals, Metals and Sustainable Development (IGF).<sup>127</sup>

Until now, most efforts toward tax transparency have focused on rights holders. While there are many good reasons to broaden the approach to include suppliers, at least two important challenges present themselves. First, many tax disclosure initiatives, such as the EITI, take place at the country level, which raises questions of how to engage non-resident suppliers, many of whom have no presence in the host country. Second, many supplier companies are not as familiar with discussions on tax accountability and transparency as rights holders who have taken part in existing mechanisms for years. Engagement with suppliers should include explaining why their inclusion is important.

125 Mali EITI, EITI Report, 2016 (2018), 12, [www.eiti.org/document/mali-eiti-report-2016](http://www.eiti.org/document/mali-eiti-report-2016).

126 NRGi, *Contract Disclosure Practice and Policy Tracker*, [docs.google.com/spreadsheets/d/1FXEeD43jw6VYHV8yS-8KJ5-rR5IOXtKxVQZBWzr-ohY/edit?userstoinvite=falltapha88%40gmail.com&ts=5e44f560-gid=0](https://docs.google.com/spreadsheets/d/1FXEeD43jw6VYHV8yS-8KJ5-rR5IOXtKxVQZBWzr-ohY/edit?userstoinvite=falltapha88%40gmail.com&ts=5e44f560-gid=0).

127 Saila Stausholm, Jaqueline Terrel and Alexandra Readhead, Intergovernmental Forum on Mining, Minerals, Metals and Sustainable Development Mining Tax Incentives Database (2019), [www.igfmining.org/tax-incentives-mining](http://www.igfmining.org/tax-incentives-mining).

#### Box 4. Where information on suppliers has improved oversight

##### Local procurement in Cameroon

Access to information about supplier identities helped two Cameroonian civil society organizations (CSOs) monitor a mining company's compliance with its contractual obligation to "use as much as possible the services and commodities from local sources as well as products manufactured in Cameroon." After establishing that the mining company hired local suppliers to provide environmental impact assessment services and dynamite, the CSOs queried why existing local suppliers did not also provide camp construction services to the company. In the absence of public reporting on supplier identities, the CSOs' analysis relied on information collected from key informant interviews. They also benefited from public access to the mining contract. The findings led the CSOs to recommend numerical targets, schedules and a monitoring framework for the use of local suppliers.<sup>128</sup>

##### Supplier registration in Iraq

In Iraq, the legal framework requires oil and gas companies to disclose details on all secondary contracts worth over USD 100 million. This includes providing the name of the company and the contract's value and signing date. When Iraq's EITI chapter cross-referenced the data with beneficial ownership information provided by the companies' registrar, it found one foreign service provider that did not register in the country—a breach of the Foreign Company Branches Law. The EITI report documented the breach and recommended that the Ministry of Oil look into the issue and investigate the beneficial ownership of the contracted company.<sup>129</sup>

##### Naftogaz oil rig procurement scandal in Ukraine

When it became public knowledge that the Ukrainian SOE Naftogaz had spent USD 400 million on a drilling platform, local journalists became interested and began to scrutinize the tender procedures, price information and companies involved. A local NGO reported that one of the winners, Highway Investment Processing, had purchased the drilling rig from a Norwegian vendor for USD 248 million—or 38 percent less than the sale price paid by Ukraine—just days before selling it to a Naftogaz subsidiary.<sup>130</sup> Media reports later found that the directors and shareholders of the winning companies were part of a network of professional nominees who held their interests through offshore shell companies.<sup>131</sup> Two of the nominees were well known in anticorruption circles as linked to hundreds of shell companies, some of which allegedly played roles in government contract and bank fraud, a U.S.-based Ponzi scheme and embargoed arms sales to African rebel groups, among others.<sup>132</sup>

128 Centre pour l'Environnement et de Développement and Réseau de Lutte contre la Faim, Monitoring local content and fiscal obligations of mining companies in Cameroon: Case of the diamond mining project of Cameroon and Korea Mining Incorporation Mobilong, East Cameroon (2011), [www.relufa.org/en/wp-content/uploads/2017/03/contractual-obligations-english.pdf](http://www.relufa.org/en/wp-content/uploads/2017/03/contractual-obligations-english.pdf).

129 EITI, *Spotlight: Transparency in the supply of goods and services in the extractive industries*.

130 Aaron Sayne, Alexandra Gillies and Andrew Watkins, *Twelve Red Flags: Corruption Risks in the Award of Extractive Sector Licenses and Contracts* (NRGI, 2017), 14-15, [www.resourcegovernance.org/analysis-tools/publications/twelve-red-flags-corruption-risks-award-extractive-sector-licenses-and](http://www.resourcegovernance.org/analysis-tools/publications/twelve-red-flags-corruption-risks-award-extractive-sector-licenses-and); Natalia Sedietska, Ukraine oil rig deal: fat cats getting fatter?, (Open Democracy, 2011), [www.opendemocracy.net/en/odr/ukraine-oil-rig-deal-fat-cats-getting-fatter/](http://www.opendemocracy.net/en/odr/ukraine-oil-rig-deal-fat-cats-getting-fatter/).

131 Graham Stack, "Why are dodgy shell companies from all over the world run by a bunch of Latvian losers?" *Ukraineleaks*, August 2014, [www.graham-stack.com/?page\\_id=119](http://www.graham-stack.com/?page_id=119)

132 Graham Stack, "Really dodgy, from arms dealing to government theft to ponzi fraud," *Ukraineleaks*, August 2014.; Gerard Ryle and Stefan Candea, "Faux Corporate Directors Stand in for Fraudsters, Despots and Spies," (International Consortium of Investigative Journalists, 2013).

## Conclusion

In light of the ongoing coronavirus pandemic and the broader energy transition away from fossil fuels, project supply chains for the extractive industries are facing multiple disruptive forces. To protect the public interest as well as their own longer-term resilience, private sector and government responses should address the supplier governance challenges detailed in this report.

As we have shown, these issues—cost control, supplier contributions to tax revenues, local procurement and corruption—are complex and interlinked. Stepping up to the challenge will require an agenda that bridges several different areas of expertise from procurement and contract management to taxation and anti-corruption.

Given the multiple uncertainties and knowledge gaps surrounding extractive industry suppliers, improving transparency is a necessary first step. Some individual rights holders, governments, SOEs and suppliers are already taking important but ad hoc steps forward. Moreover, as we explore in annex 1, a number of international transparency and reporting initiatives are beginning to produce guidance on these issues.

As a result of this progress, important precedents exist for transparency around procurement processes, supplier identities, spending on suppliers and supplier taxation. In some contexts, this information is already being used to improve oversight and accountability. But making these disclosures more widespread, consistent and useful will require specific actions from many stakeholders, including affected citizens, public oversight actors, governments, rights holders, SOEs and suppliers themselves.

Civil society, journalists, the international community, home country governments and financiers need to increasingly inquire about the economic impacts and risks associated with extractive industry suppliers. They need to produce more research and stronger good practice recommendations on the frontier issues discussed in this report, such as the public accountability of cost audits and local procurement, approaches to supplier taxation and combatting supplier-related corruption.

Host country governments need to assess whether information flows around their oil, gas and mining projects are adequate for effective public oversight, and take steps to improve these where necessary. Where they take an active role in planning or approving supplier selection, governments should question whether adequate safeguards exist to protect against conflicts of interest. This is particularly pertinent where they engage in the extractive industries via SOEs.

Rights-holding companies should proactively provide information about their suppliers and establish expectations of transparency and accountability throughout their supply chains. They should consider the economic and integrity impacts of suppliers in their due diligence processes that accompany supplier selection. Suppliers should also embrace increased transparency, using it as an opportunity to improve operational and sustainability outcomes.



Global reporting and transparency initiatives have an important role to play in convening dialogue and stimulating progress on these issues. Unresolved transparency challenges include the coordination and standardization of definitions and approaches, establishing practical reporting thresholds and achieving disclosures at the different levels where the information is needed most (project, national or companywide).

Active engagement from supplier companies will be essential to uncovering viable ways forward in these and other areas. Importantly, new conversations among the main stakeholders identified in this report are necessary to ensure this crucial area of extractive industry governance finally gets the attention it deserves.

## Appendix. Notes on spending estimates for suppliers

We based our spending estimates for suppliers in figures 1 and 2 of this report on our analysis of data from the Rystad Energy: ServiceCube and UCube and S&P Global: Mine Economics databases.<sup>133</sup> All figures are nominal USD. We split all asset-level operational and capital expenditures between two categories: “goods and services from suppliers” and internal spending on “employees and overheads.” As asset-level data, it is important to note that they do not cover midstream and downstream expenditures such as construction of transport and storage facilities, or company headquarters expenditures that are not accounted to a specific project including certain financing costs and professional services fees.

**Petroleum.** The ServiceCube and UCube databases reflect Rystad analysis of 65,000 fields, covering all known petroleum assets globally. The data sources for each category in figure 1 are:

- **Goods and services suppliers.** All categories except “internal spend” in Service Demand Cube.
- **Employees and overheads.** The “internal spend” category in Service Demand Cube, consisting of salaries and selling, general and administrative expenses.<sup>134</sup>
- **Government revenue.** The government take category in U Cube economic model, consisting of royalties, income taxes and government/national oil company shares of production.
- **Investor returns.** The free cash flow category in the U Cube economic model.

**Mining.** At the time of analysis, the S&P Mine Economics database reflected 1,390 mining assets globally, with the following coverage of key global commodities: copper–87 percent; cobalt–88 percent; gold–65 percent; iron ore–81 percent; lead–50 percent; lithium–90 percent; molybdenum–55 percent; nickel–64 percent; palladium–100 percent; platinum–94 percent; rhodium–93 percent; silver–77 percent; zinc–68 percent; and U3O8–66 percent. Data sources for each category in figure 1 are:

<sup>133</sup> For detailed description of data methodology of each platform, please see: Rystad Energy, Client Portal: Documentation and Methodology; S&P Global, *Mine Economics methodology*, platform. [marketintelligence.spglobal.com/help/Mine\\_Economics\\_Methodology.htm](https://marketintelligence.spglobal.com/help/Mine_Economics_Methodology.htm).

<sup>134</sup> The sum of Service Demand Cube expenditures on goods and services from suppliers and internal and overheads closely match with operational and capital expenditures from the U Cube economic model. Small differences are due to reporting differences and possible minor expenditure categories not captured by Service Demand Cube.

- **Goods and services suppliers.** Supplier expenditure figures are not available in the Mine Economics database. We therefore estimated the proportion of expenditures that goes towards suppliers across the nine cost categories contained in the Mine Economics database. (See table 2 below.) The estimates are based on interviews with S&P Global experts, industry experts and market analysis reports.<sup>135</sup>
- **Employees and overheads.** Reflects the remainder in each cost category of the Mine Economics database after deducting the estimated share spent with suppliers.
- **Government revenues.** Royalties and tax categories in Mine Economics database.
- **Investor returns.** Post-tax cash flow category in Mine Economics database.

Est. share of expenditure with suppliers:	
Labor cost	30%
Electricity cost	80%
Fuel cost	90%
Reagents (including acid) cost	90%
Other cost	70%
Non-ferrous: realization costs	90%
Indirect and extraordinary costs	30%
Sustaining capex	60%
Development and expansion capex	80%

Table 2. Estimated proportion of S&P Mine Economics spending categories spent on suppliers

<sup>135</sup> Valentina Ruiz Leotaud, "Underground mining equipment market to reach \$30.5 billion by 2023," Mining.com, 13 September 2016, [www.mining.com/underground-mining-equipment-market-to-grow-says-report-while-big-players-struggle](http://www.mining.com/underground-mining-equipment-market-to-grow-says-report-while-big-players-struggle); and PwC, *Mine* (2017), [www.pwc.com.au/publications/pdf/global-mine-2017.pdf](http://www.pwc.com.au/publications/pdf/global-mine-2017.pdf).

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