

Preface

An Introduction to Corporate Social Responsibility in the Extractive Industries

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Mr. Smith was invited to deliver the keynote speech at the Yale Human Rights & Development Law Journal's Symposium on Corporate Social Responsibility in the Extractive Industries, at Yale Law School, on March 8, 2008. The following Preface is based on that speech.

I. INTRODUCTION

Many congratulations to the Board and staff of the *Yale Human Rights & Development Law Journal* for hosting this timely and important Symposium on Corporate Social Responsibility in the Extractive Industries, and for devoting this volume of the *Journal* to an in-depth analysis of the key issues addressed in the Symposium.

This Preface is designed to paint a broad Corporate Social Responsibility (CSR) backdrop for this special volume and to provide a context for the more detailed articles that follow. To that end, it defines the concept of CSR, particularly as it relates to the extractive industries, and identifies the primary business drivers behind it. In addition, this introduction highlights some of the key CSR issues facing the extractive industries today and in the coming years, and previews how the

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succeeding articles may help to resolve them.

II. THE YIN AND YANG OF CSR

One of the challenges of working in the relatively new field of CSR is that people have highly varied perspectives regarding what CSR means and entails. Some view CSR as a form of philanthropy, others as a public relations exercise. Some regard it as a type of corporate volunteerism, others as a guideline for risk management.

For the purposes of this Preface, I propose employing the definition put forward by former U.N. Secretary General Kofi Annan. According to Mr. Annan, CSR is a business concept embraced in the 1990s pursuant to which corporations seek to responsibly address social and environmental issues raised in the course of business through support for international norms and sustainable practices. Norms and sustainable practices of particular focus include broad-based human rights, labor rights, and the rights of indigenous peoples; environmental stewardship; and transparency.¹

In essence, CSR is a by-product of corporate globalization. It reflects the yin and yang of the advantages of, and the concerns regarding, the impact of globalization.

To multinational companies, globalization is the cornerstone of business in the new millennium. It provides the opportunity to explore new regions of production, increase efficiency, spur business growth, and augment the rate of return to shareholders. Many industry leaders regard CSR initiatives as a means of managing attendant legal and reputational risks.

Some stakeholders, however, worry that globalization can also lead to less beneficial ends. Specific concerns include the potential for exploitation of workers and the environment, the diminution of respect for human rights, and the fueling of global inequalities. With respect to the extractive sector, this is a particular concern in relation to what has been identified as the "resource curse," a phenomenon explored in depth in this volume.

Indicators that contribute to such concerns include that while the wealth of developed countries and their citizens continues to grow, due in no small part to the business activities of their multinational companies, the relative wealth of many developing countries and their citizens continues to shrink -- despite the fact that these nations provide many of the resources essential to sustaining the developed world. Of the 100 largest economies in the world, most are multinational companies, a

1. See Kofi Annan, Sec'y-Gen., United Nations, Address to World Economic Forum, Jan. 28, 2001, http://www.un.org/News/dh/latest/address_2001.htm; Kofi Annan, Sec'y-Gen., United Nations, Address to World Economic Forum, Jan. 31, 1999, http://www.un.org/News/oss/sg/stories/statments_search_full.asp?statID=22.

number of which are members of the extractive sector.² Three hundred multinationals currently account for 25% of the world's total assets, and only 21 nations have gross domestic products that exceed the annual sales of each of the six largest multinationals.³

These statistics are relevant to CSR because they underscore the global economic impact of multinational companies. The inequalities highlighted also establish the challenging political context facing today's business leaders as they seek to operate at an international level, particularly in developing nations where the absence of government transparency can lead to an extreme variance in standards of living. Concerns regarding such inequalities, combined with questions regarding the environmental and the social impact of globalization, are putting members of the extractive industry under increased scrutiny by customers, shareholders, and governments and subjecting them to new risks in the marketplace.

Whether corporate globalization helps to resolve economic disparities by providing jobs, education, and raising living standards, or merely serves to exacerbate these inequalities, is an important business matter. To secure a social license to operate, it is imperative that members of the extractive sector promote the social and environmental normative standards identified by Mr. Annan in a way that is visible to local and international stakeholders.

This imperative is particularly the case when multinationals operate in countries with weak governments that lack the capacity or the political will to fulfill their responsibilities. In these cases, stakeholders often look to multinationals to "fill the gap" regarding worker protections, environmental standards, and respect for human rights.

Indeed, with the price of oil and precious metals at all-time highs, there are sometimes additional local expectations that multinationals will assume governmental functions, from building hospitals and roads, to providing for clean water and educational systems. The assumption of such responsibilities can create a slippery slope, and companies need to assess how to balance their CSR responsibilities to local communities without establishing unsustainable dependencies or overstepping their private sector roles.

In this New World Order, multinationals are also held to higher standards of accountability than they were only a few decades ago. On the global media stage, companies in the extractive sector are no longer regarded as responsible solely for their own behavior, but sometimes also for the behavior of those with whom they are associated—including host governments, partners, and contractors. Many companies, for example, have been charged in lawsuits brought under the Alien Tort Claims Act with complicity in human rights abuses allegedly committed by the governments with which they were working.⁴

2. BRUCE PIASECKI, *WORLD INC.* 4 (2007).

3. *Id.*

4. *See, e.g., Khulumani v. Barclay Nat'l Bank Ltd.*, 504 F.3d 254 (2d Cir. 2007) (*per curiam*);

Moreover, the behavior of multinationals in the industry is increasingly assessed not just under local law, but pursuant to international normative standards, such as the Universal Declaration on Human Rights and conventions by the International Labor Organization, and best industry practices, such as the Voluntary Principles on Security and Human Rights (the “Voluntary Principles”) and the Extractive Industries Transparency Initiative.

In addition to these overarching reasons for members of the industry to be sensitive to CSR issues, there are also a plethora of more specific CSR business drivers. One set of business drivers encourages companies to enhance their products and services. CSR initiatives respond to these drivers by seeking to promote brand image, customer loyalty, employee recruitment and retention, and positive community relations.

Another set of business drivers requires the management of risks that create legal and reputational exposure. Responses to such risks include CSR initiatives designed to avoid divestment campaigns, boycotts, hostile shareholder resolutions, attacks on corporate property, campaigns to have the company delisted from stock exchanges, sanctions laws, and lawsuits under the Alien Tort Claims Act. Indeed, concerns regarding the roles and responsibilities of extractive sector companies operating in foreign nations, and associated potential liabilities under the Alien Tort Claims Act, led to the creation of the Voluntary Principles, which have since become the standard for industry behavior related to the nexus of security and human rights.

In light of these developments, many CEOs in the extractive sector have come to believe that the future of globalization, as well as the success of particular projects, is tied to whether companies conduct business in a manner acceptable to those affected by it. For this reason, effective and meaningful CSR policies are increasingly regarded as a necessary prerequisite to securing a social license to operate and, when appropriately implemented, to helping companies address the risks of globalization in a way that benefits all stakeholders.

III. CSR CHALLENGES FACING THE EXTRACTIVE INDUSTRIES

Multinationals in the extractive sector face many of the same CSR challenges encountered by other global industries. These include environmental, corporate governance, transparency, and worker rights issues, as well as broad-based human rights concerns.

Members of the industry also face some relatively distinctive challenges. Unlike manufacturing companies, which can choose where to set up operations based on a number of predetermined business variables,

Sarei v. Rio Tinto, PLC, 487 F.3d 1193 (9th Cir. 2007); Romero v. Drummond Co., No. CV-03-BE-0575-W, 2006 WL 5186500 (N.D. Ala. 2006).

companies in the extractive industries do not have the option of choosing where gold, oil, diamonds, or gas are located. Sometimes these assets are found in failed states and conflict zones, where there is little or no rule of law and corruption is unchecked. Sometimes the resources are located in pristine rainforests or in areas inhabited by indigenous peoples. Such factors raise a host of issues that a company seeking to be socially responsible must address.

The Symposium featured four panels that addressed these and other cutting-edge CSR issues.

The first panel, *Corporations, Developing Countries, and the Resource Curse*, focused upon the challenges facing members of the extractive sector seeking to conduct business responsibly in developing nations and the associated challenges confronting the governments of those nations as they seek to profit from their own resources.

The past few decades have provided resource-rich countries with unprecedented opportunities for economic growth and social prosperity. The price of oil, for example, increased from U.S. \$ 3 per barrel in 1973⁵ to more than U.S. \$ 130 per barrel in mid 2008,⁶ constituting one of the largest capitol transfers ever to accrue in such a short time span. Yet most of these nations were unable to harness their economic windfalls in a productive manner. To the contrary, the record indicates that countries lacking oil and mineral resources had much stronger Gross Domestic Product growth per capita than resource rich countries, and that the governments with the most abundant resources did little to improve the lives of their citizens. Indeed, many such governments lack the capacity, and sometimes also the political will, to effectively guarantee rule of law, accountability, and transparency – including with respect to the revenue streams generated by extractive sector operations.

These issues provide unique challenges for a company in the extractive sector as it seeks to balance its role as a corporate guest in a host nation with the needs of that nation's populace for more effective governance and a voice with respect to the allotment of its resources. Articles from members of the first panel address these critical issues.

The second panel, *Legalism vs. Voluntarism: Assessing Modes of Corporate Social Responsibility in the Extractive Sector*, addressed the underlying debate regarding the relative effectiveness of embedding CSR objectives in the rule of law or pursuing them through voluntary company codes of conduct and industry initiatives.

Today, most of the "majors" in the extractive sector have adopted internal codes of conduct governing corporate compliance issues ranging from the environmental stewardship to respect for worker rights. Many also participate in industry initiatives, such as the Voluntary Principles,

5. See, e.g., Jonathan Bernstein, *Oil Soaked*, ETFZONE, Mar. 1, 2008, http://www.etfzone.com/?template=viewarticle&article_id=889.

6. See, e.g., *Oil Crosses \$130 a Barrel for the First Time*, CNN.COM, May 21, 2008, <http://money.cnn.com/2008/05/21/markets/oil.ap/index.htm?cnn=yes>.

which provide guidance for companies regarding balancing the need for security with respect for human rights, and the Extractive Industries Transparency Initiative, which is designed to help companies and governments promote transparency with respect to revenue streams. Companies also participate in multi-sectoral initiatives, such as the United Nations' Global Compact, which provides guidance regarding human rights, labor rights, environmental stewardship, and transparency.

Some stakeholders, however, question the degree to which such voluntary initiatives promote accountability. In particular, some believe that local regulation is more effective at driving positive CSR behavior. Articles from members of the second panel challenge whether voluntary initiatives are successful in shaping corporate behavior and whether recourse to local legal mechanisms is the only manner in which stakeholders adversely impacted by corporate ventures can protect their rights and interests.

The third panel, titled *The Engagement Paradox: Should Extractive Industry Corporations Do Business in Failed States and Conflict Zones?*, focused upon the fundamental issue of whether companies should conduct business in countries and regions in conflict.

Repressive governments, civil wars, insurgencies, corruption, and interethnic violence impact business operations and create human rights responsibilities and liabilities for multinationals. Accordingly, whether to enter a country and conduct business with a particular government is a baseline question for members of the extractive industry. Should multinationals operate in countries with repressive regimes? Is it reasonable to draw a distinction between working with governments with merely "problematic" human rights records and those that the international community has deemed pariah states? If crises occur after the establishment of operations, is it more responsible for a company to maintain its presence or to disengage? These are some of the most difficult CSR issues facing the extractive sector. Articles from members of the third panel consider these and other issues through the prism of past and prospective extractive sector projects in some of the world's more challenging conflict zones.

The fourth panel, *The Future of Corporate Social Responsibility*, explored the direction in which CSR is moving by projecting how outstanding challenges for companies, governments, and other stakeholders are likely to be resolved in the coming years.

Managing the nexus of human rights and security is one of the most demanding CSR issues for members of the industry and is certain to be a continuing area of interest. Virtually all of the Alien Tort Claims Act cases against multinationals in the extractive sector are premised upon allegations that defendant companies conspired with or aided and abetted human rights abuses conducted by public security forces.

Does providing a revenue stream to a repressive regime make a company complicit in that government's abuses? Is it possible to work

with such governments without being regarded as aiding and abetting in their human rights abuses? Efforts to define the parameters of corporate complicity with respect to human rights abuses, and a company's legitimate sphere of influence—whether by the courts, the Congress, or intellectual leaders such as John Ruggie, the U.N. Special Representative on Transnational Corporations and Human Rights—could provide greater certainty for both multinationals and impacted stakeholders.

Similarly, the Voluntary Principles offer important guidance for companies with respect to security arrangements with public and private security forces, but many participating companies remain uncertain regarding how best to operationalize these guidelines and ensure that they are effectively monitored. The development of best practices with respect to the Voluntary Principles, as well as Human Rights Impact Assessments, would provide important guidance for the industry.

More generally, pending tensions between international law and voluntary initiatives, as well as between governments seeking to dictate the development of their resources and impacted communities demanding the right to “free prior and informed consent,” will influence the concept of social responsibility and corporate risk management initiatives. The fact that private sector actors play by a more demanding set of rules than the parastatals against which they compete, will also impact upon the success of current initiatives and help to shape the future of CSR.

Articles from members of the fourth panel reflect upon these and other CSR challenges, and offer proposals by which to resolve them.

IV. CONCLUSION

The aforementioned CSR issues are of considerable interest to multinationals, governments, and stakeholders alike. It is important that they be addressed, and the Symposium and this special volume of the *Yale Human Rights & Development Law Journal* provide welcome fora for critical thought and analysis. Congratulations, again, and many thanks to the *Journal's* Editors and Board.

