Annual report 2006

Council on Ethics for the Government Pension Fund – Global

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Government Pension Fund – Global

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Introduction

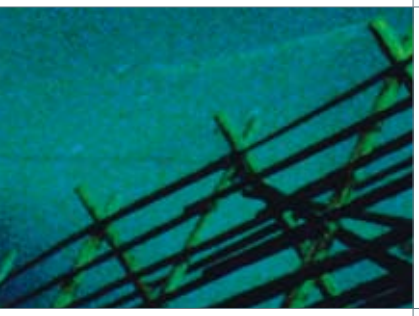
The Council on Ethics for the *Norwegian Government Pension Fund – Global* (previously the Government Petroleum Fund) was established by government decision on 19 November 2004, simultaneously with the implementation of the Fund's Ethical Guidelines. The Council on Ethics is an independent advisory body charged with submitting recommendations to the Ministry of Finance. Our mandate is to assess whether companies should be excluded from the *Norwegian Government Pension Fund – Global* because of acts or omissions that are in conflict with the criteria of the Ethical Guidelines. The Council has held 12 meetings in 2006.

During the Council's first year in operation (2005), many of its efforts centred on an initial screening aimed at identifying companies involved in the production of weapon types that are inconsistent with the Guidelines. Besides weapons banned by international law, these include nuclear weapons and cluster munitions. In 2006 we have focused to a greater extent on human rights, including labour rights, and environmental issues. The first recommendations on a subject establish a precedent for how similar cases will be treated in the future. We have taken great care to ensure that the recommendations are thorough, well documented and of good quality, as we consider this to have a bearing on the long-term impact of the Ethical Guidelines of the *Norwegian Government Pension Fund – Global*. Some of the Council's recommendations have attracted a great deal of attention. We believe that the extensive documentation and the in-depth discussions in our recommendations have contributed to improving the foundation for decisions made by other funds with similar ethical criteria.

According to its mandate, the Council on Ethics shall submit an annual report describing its activities to the Ministry of Finance. A large part of the Council's work is reflected in our recommendations, which are reproduced unabridged in this Annual Report. When the Council decides to examine a case more closely, it may take six to eighteen months before a recommendation is published. Part of the work done in 2006 will therefore not be published until next year's Annual Report.

This report includes the five recommendations made public by the Ministry from 6 January 2006 to year's end. In accordance with the criteria of the Guidelines we have recommended the exclusion of one company on the basis of unacceptable working conditions, particularly within the company's supplier network. Another company, which previously had been excluded because of offshore oil exploration activities in the non-autonomous territory of Western Sahara, has been recommended for reintroduction into the Fund's investment universe because the exploration activity has ceased. In 2006 we also submitted our first recommendation on exclusion of a company due to unacceptable risk of complicity in severe environmental damage. This refers to a mining company that practices riverine tailings disposal. Moreover, we have reviewed the basis for the recommendation to exclude a company that no longer contributes to the production of cluster weapons, but is currently involved in the production of nuclear weapons. Finally, we have recommended the exclusion of a company on the grounds of production of cluster munitions.

The Ministry of Finance has decided to adopt these recommendations. In the Annual



Report we have also included two letters to the Ministry of Finance which are not formally considered conclusive recommendations. Investigations regarding the operations of individual companies in these cases are not as detailed as those of companies recommended for exclusion, because the activities in question probably do not imply ongoing breaches of the Guidelines.

The Council has a Secretariat with a staff of five whose job is to collect and quality assure documentation, as well as facilitate the Council's decision-making process. References, e.g. in the form of footnotes, are used to indicate the sources relied upon in each recommendation.

In 2006 much effort has been made to systematize the information gathering on companies in the Fund. Among other measures, we have entered into an agreement with the British research provider EIRiS to monitor the Fund's portfolio with a view to identifying companies that may have operations that counter the Guidelines. In addition to what is found in publicly available sources, there is often a need to throw more light on certain matters. To this end the Council engages professionals from consultancy firms, research institutions, non-governmental organisations, etc., often in the country where the alleged breaches of the Guidelines occur. The Council places great importance on assuring the quality and confidentiality of such work.

A great part of the Council on Ethics and the Secretariat's work never appears in official documents since many assessed companies are not, for a variety of reasons, proposed to be excluded from the Fund. Many cases are already closed during preliminary investigations. However, information which at first is insufficient to render a complete assessment of a company may be brought up again if new factors come to our knowledge at a later stage. The Council on Ethics prioritizes cases in which exclusion seems most probable, stressing the gravity of the situation, whether a company is accused of several unethical practices, whether it is probable that these practices will continue, and the possibilities of substantiating the accusations levelled against the company. The aim is to identify companies that constitute an unacceptable risk of gross violations of the Ethical Guidelines, at present or in the future. During the past year the Council has assessed approximately 70 companies.

The issue of corporate responsibility for compliance in human rights violations is at the centre of the Council's work, being a legally and ethically important question also in international research. In October 2006 the Council hosted an international seminar to throw light on issues related to corporate responsibility for human rights violations. We found it very rewarding to invite international experts in the field to discuss this topic with us. The seminar is described in further detail later in this Annual Report.

We appreciate the contact established with several research institutions, non-governmental organisations and media representatives, and would like to express our thanks for all questions, comments, ideas and suggestions received in the past year.

Gro Nystuen (Chair) Andreas Føllesdal Anne Lill Gade Ola Mestad Bjørn Østbø

Overview of Recommendations issued by the Council on Ethics

Published after 6 January 2006

15.11.05 Recommendation on exclusion of Wal-Mart Stores Inc.
Recommendation on the exclusion of US retailer Wal-Mart Stores Inc. because of unacceptable working conditions both in some of the company's own stores and among suppliers.
(Published 6 June 2006.)

15.02.06 Recommendation on exclusion of Freeport McMoRan Copper & Gold Inc.
Recommendation on the exclusion of US mining company Freeport McMoRan Copper & Gold Inc. owing to environmental damage caused by the company's mining operation through tailings disposal into a natural river system.
(*Published 6 June 2006.)*

18.04.06 Reviewed basis for exclusion of EADS Co.
Recommendation on continued exclusion of the French company EADS Co. (European Aeronautic Defence and Space Company), but the basis for exclusion has been changed from production of key components for cluster munitions to production of key components for nuclear weapons.
(Published 18 April 2006.)

24.05.06 Recommendation to revoke the exclusion of KerrMcGee Corporation
Recommendation to revoke the exclusion of US oil company KerrMcGee Corporation because the company no longer is involved in offshore exploration activities in Western Sahara, a non-autonomous territory.
(*Published 1 September 2006.)*

06.09.06 Recommendation on exclusion of Poongsan Corporation
Recommendation on exclusion of the Korean company Poongsan Corporation owing to its involvement in the production of key components for cluster weapons.
(*Published 6 December 2006.)*

The Ministry of Finance has adhered to the Council's recommendations.

22.03.06 Letter to the Ministry of Finance on Aracruz Celulose S.A.

15.05.06 Letter to the Ministry of Finance on investments connected to the Middle East

Members of the Council and of the Secretariat

The Council on Ethics

Gro Nystuen (Chair), dr. juris and Associate Professor at the Center for Human Rights, the University of Oslo
Andreas Føllesdal professor PhD in Philosophy at the Center for Human Rights, the University of Oslo
Anne Lill Gade MSc in limnology (freshwater ecology), Product Safety Manager at Jotun AS
Ola Mestad dr. juris and Professor at the Centre for European Law, University of Oslo
Bjørn Østbø economist HAE, Chief Executive Officer at Vital Eiendom AS

The Secretariat

The Council has a Secretariat that investigates and prepares cases for the Council.
At the end of the year, the Secretariat had the following employees:
Pia Rudolfsson Goyer (cand. jur, LLM)
Hilde Jervan (cand. agric)
Eli Lund (economist)
Aslak Skancke (graduate engineer)
Kamil Zabielski (post graduate student)

Mandate for the Government Pension Fund – Global's Council on Ethics

"In the Revised National Budget for 2004, the Ministry of Finance presented ethical guidelines for the Government Petroleum Fund (now the *Government Pension Fund – Global*). The Norwegian Parliament endorsed the guidelines in Budget Recommendation to the Storting No. 1 (2003-2004). The Ministry of Finance established the Guidelines which entered into force 1 December 2004.

The guidelines establish the following tasks for the Council on Ethics:
The Council on Ethics shall consist of five members. The Council shall have its own secretariat. The Council shall submit an annual report on its activities to the Ministry of Finance.

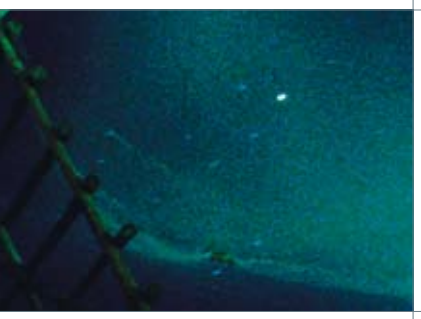
Upon request of the Ministry of Finance, the Council issues recommendations on whether an investment may constitute a violation of Norway's obligations under international law.

The Council shall issue recommendations on negative screening of one or several companies on the basis of production of weapons that through normal use may violate fundamental humanitarian principles. The Council shall issue recommendations on the exclusion of one or several companies from the investment universe because of acts or omissions that constitute an unacceptable risk that the Fund contributes to:

- Serious or systematic human rights violations, such as murder, torture, deprivation of liberty, forced labour, the worst forms of child labour and other forms of child exploitation
- Serious violations violations of individual rights in war and conflict
- Severe environmental damages
- Gross corruption
- Other particularly serious violations of fundamental ethical norms

The Council shall raise issues under this provision on its own initiative or at the request of the Ministry of Finance.

The Council is to gather the necessary information on an independent basis and ensure that the matter is elucidated as fully as possible before a recommendation concerning screening or exclusion from the investment universe is issued. The Council can request Norges Bank to provide information as to how specific companies are dealt with in the exercise of ownership rights. All enquiries to such companies shall be channelled through Norges Bank. If the Council is considering a recommendation to exclude, the draft recommendation, and the grounds for it, shall be submitted to the company for comment.



The Council shall review on a regular basis whether the grounds for exclusion still apply and can on receipt of new information recommend that the Ministry of Finance reverse the exclusion decision.

See the Revised National Budget for 2004 for an elaboration of the ethical guidelines and of the Council's tasks.

According to the ethical guidelines, the recommendations of the Council on Ethics and the decisions of the Ministry of Finance are made public. The Ministry may in special cases defer the date of publication if this is deemed necessary to assure due and proper disinvestment from a financial point of view. Against this background, and in regard to the Council's recommendations, the Ministry of Finance is the appropriate body to approve or reject requests to examine documents under the Freedom of Information Act.

The Ministry of Finance determines the Council members' and the secretaries' remuneration as well as the Council's budget. The Ministry of Finance shall be the contractual counterparty to any agreement the Council needs to enter into with other parties.

The Ministry of Finance may make additions to or changes in this mandate."

In accordance with a letter from the Ministry of Finance of 24 October 2005, the Council shall submit to the Ministry of Finance a letter with recommendations on fixed dates four times per year (15 February, 15 May, 15 August and 15 November). If the Ministry, on the basis of the recommendations by the Council, decides upon exclusion of companies, the Norwegian Central Bank shall have two entire months to dispose of any securities in the company held by the Fund. The Ministry will publish recommendations and decisions regarding any exclusion after the completion of such disposal.

Companies the Ministry of Finance has decided to exclude from the Government Pension Fund – Global

Cluster Weapons

- Alliant Techsystems Inc.
- General Dynamics Corp.
- L3 Communicaionts Holdings Inc.
- Lockheed Martin Corp.
- Poongsan Corp.
- Raytheon Co.
- Thales S.A.

Nuclear Weapons

- BAE Systems Plc, Boeing Co.
- EADS Co.
- EADS Finance B.V.
- Finmeccanica Sp.A.
- Honeywell International Corp.
- Northrop Grumman Corp.
- Safran S.A.
- United Technologies Corp.

Anti Personell Landmines

- Singapore Technologies Engineering

Human Rights

- Wal-Mart Stores Inc.
- Wal-Mart de Mexico S.A.

Environmental Damage

- Freeport McMoRan Copper & Gold Inc.

Kristin Halvorsen
Gro Nystuen
Ola Mestad
Andreas Føllesdal
Simon Chesterman
John Ruggie

Seminar on Corporate Complicity in Human Rights Violations

The Ethical Guidelines of the Government Pension Fund require that the Council, among other things, recommend disinvestment from companies when there is an unacceptable risk that they might contribute to serious or systematic human rights violations. With a view to exploring the theoretical and practical aspects of this very complex legal and philosophical topic, the Council invited a number of scholars and practitioners to a two day seminar in Oslo on 23rd–24th October, 2006.

The workshop, which was opened by the Norwegian Minister of Finance, Kristin Halvorsen, provided an opportunity for in depth discussions on the topic of corporate complicity and human rights from several different perspectives, including international law, human rights law, national tort and criminal law, philosophy and ethics, as well as investors' and corporate perspectives. Approximately 50 participants with these different backgrounds met over the 2 day seminar to discuss the extent to which companies, as well as investors, may be legally or ethically responsible for contributing to human rights abuses in what is sometimes called their "sphere of influence".

Keynote speakers included Harvard Professor and Special Representative to the UN Secretary General on Business and Human Rights, John Ruggie (SRSG), together with members of the Council (Gro Nystuen, Ola Mestad og Andreas Føllesdal) as well as Simon Chesterman (New York University School of Law), Christopher Kutz (University of California – Berkeley), Henrik Syse (Norges Bank), Paul Munn (Hermes), Bruno Demeyre (Katholieke Universiteit Leuven), Marinn Carlson (Sidley Austin LLP), Urs Gasser (University of St. Gallen), David Rodin (Oxford Centre for Applied Ethics) and Pernilla Klein (AP3). Madeleine Albright (Albright Group) addressed the seminar in a keynote dinner speech.

The contributions and discussions addressed both general aspects related to the topic as well as the two publicised recommendations issued by the Council on Ethics regarding specific companies' alleged complicity in human rights violations, namely the Total recommendation (publicised in the 2005 annual report) and the Wal-Mart recommendation (publicised in this annual report). It was of great value to the Council to get so much highly qualified input on how to implement the human rights criteria. It is likely that the Council will arrange seminars on similar issues related to the Council´s work also in the future.

The Recommendations

To The Ministry of Finance

Oslo, November 15, 2005
(Published June 6, 2006)

Recommendation on exclusion of Wal-Mart Stores Inc.

Contents

1 Introduction

The Council on Ethics for the Norwegian Government Petroleum Fund decided at a meeting 27 June 2005 to consider whether the business of Wal-Mart Stores Inc. (Wal-Mart) might entail complicity by the Fund in serious or systematic violations of human rights under Point. 4.4 of the Ethical Guidelines.

As of 31 December 2004, the market value of the Government Petroleum Fund's shareholding in Wal-Mart was NOK 1,656 billion and in Wal-Mart de Mexico S.A. NOK 72.9 million. The market value of the Fund's bond holding in Wal-Mart was NOK 668.6 million.

Wal-Mart is alleged to run its business operations in a manner that contradicts internationally recognised human rights and labour rights standards, both through its suppliers in a number of countries in Asia, Africa and Latin America, and in its own operations. There are numerous reports alleging that Wal-Mart consistently and systematically employs minors in contravention of international rules, that working conditions at many of its suppliers are dangerous or health-hazardous, that workers are pressured into working overtime without compensation, that the company systematically discriminates against women with regard to pay, that all attempts by the company's employees to unionise are stopped, that employees are in some cases unreasonably punished and locked up, along with a number of other allegations which will be subject to further discussion below under section 4.

The Council has, in accordance with point 4.5 of the Ethical Guidelines, (through Norges Bank in a letter dated 14 September 2005), asked Wal-Mart and Wal-Mart de Mexico S.A., to comment on the above allegations and the background for them. These enquiries were not answered.

In order to ascertain any risk of complicity in serious or systematic human rights violations there must, according to the Council's understanding of the Ethical Guidelines, exist a direct link between the company's operations and the relevant violations. A further criterion is that the violations have been committed to serve the interests of the company and that the company has been aware of the violations, but has omitted to take steps to prevent them. There must be an unacceptable risk either that the violations are presently taking place or will take place in the future. The Council considers that all these conditions are met in the case at hand. The Council's conclusion is that the Ethical Guidelines, Point 4.4., first alternative, provide a basis for recommending exclusion of Wal-Mart because of the risk of complicity in serious or systematic violations of human rights.

2 Background

Wal-Mart is the world's largest retailer with a turnover in 2005 in excess of 285 billion USD. In Mexico, the company operates through its subsidiary Wal-Mart de Mexico S.A. Wal- Mart's stake in Wal-Mart de Mexico S.A. is about 62 %.[1]

Wal-Mart runs stores and shopping centres under the names Wal-Mart Stores, Supercenters, Neighborhood Markets and Sam's Club. The company sells, inter alia, garments, footwear, foodstuffs, household appliances and electronic goods. Wal-Mart also profiles itself through low price sales and has sales outlets in the USA, Canada, Argentina, Brazil, Germany, Mexico, Korea, the United Kingdom and Puerto Rico.[2] The company also runs sales operations in China through joint venture agreements. Wal-Mart imports products

from 70 countries around the world.[3] The Council has been apprised of a large number of allegations that parts of Wal-Mart's business operations are run in an ethically unacceptable manner. These refer in part to working conditions of employees at the company itself, and in part to unacceptable working conditions at the company's suppliers.

The Council's secretariat has been investigating these conditions since medio 2005. In order to distinguish between unacceptable conditions connected with the company's own operations and conditions linked to the supplier chain, the two are considered seperately in the following:

- Conditions in the company's global supplier network. Examples are given in section 4.1.
- Conditions referring to the company's own operations, mostly in North America. Examples are given in section 4.2.

A large amount of information on various allegations regarding Wal-Mart's operations are available. The present recommendation presents a selection of examples. The selection has been made to show the breadth of cases, both in terms of conditions within the company and its supplier chain, and in terms of the large geographical spread and the large volume of cases related to Wal-Mart.

Publicly available sources such as newspapers and magazines have been relied upon, as well as information emerging in connection with a number of lawsuits against Wal-Mart concerning conditions in the supply chain in poor countries as well as conditions in the company's own business operations in North America. On commission from the Council, information has also been obtained from lawyers, various organisations and individuals. Certain parts of this source base will, at the request of the sources involved, not be made public.

The Council's task is to establish whether there exists an unacceptable risk of complicity in violations of international standards. In other words, the Council does not consider it necessary to find proof of the veracity of each individual claim emerging from the material available to the Council.

3 The Council's considerations

The Council has to consider whether the Government Petroleum Fund can be said to contribute to unethical acts or omissions through its ownership in Wal-Mart. Point 4.4., second paragraph, first bullet point of the Ethical Guidelines states:

"The Council shall issue recommendations on the exclusion of one or more companies from the investment universe because of acts or omissions that constitute an unacceptable risk of the Fund contributing to: Serious or systematic human rights violations, such as murder, torture, deprivation of liberty, forced labour, the worst forms of child labour and other forms of child exploitation."

The Council will consider the question of excluding Wal-Mart under this provision. The other alternatives in Point 4.4., regarding violations of individuals' rights in war or conflict, severe environmental damage, gross corruption or violation of other ethical norms, are considered less relevant to the case at hand.

3.1 Point 4.4, second paragraph, first bullet point

Point 4.4, second paragraph, first bullet point contains a general reference to human rights. NOU (Norwegian Official Report) 2003: 22, which is the basis on which the Ethical Guidelines were drafted, states: *"Companies' contributions to serious or systematic violation of human rights and labour rights should, in the Committee's opinion be encompassed by the proposed exclusion mechanism."*[4] Where the scope of the terms human rights and complicity are concerned, the Council stated the following in its recommendation regarding Total S.A., issued on 15 November 2005:[5]

"The Council takes as its point of departure that the reference to human rights pertains to internationally recognised human rights and labour rights. It is clear from the wording of this provision that the specific human rights violations listed are examples of such violations and not an exhaustive list.

Not all human rights violations or breaches of international labour rights standards fall within the scope of the provision. Point 4.4. states that human rights violations must be "serious or systematic". The Graver Committee recommends "fairly restrictive criteria for deciding which companies should be subject to possible exclusion …".[6] *The Council assumes that a determination of whether human rights violations qualify as serious or systematic needs to be related to the specific case at hand. However, it seems clear that a limited number of violations could suffice if they are very serious, while the character of a violation need not be equally serious if it is perpetrated in a systematic manner.*

Only states can violate human rights directly. Companies can, as indicated in Point 4.4., contribute to human rights violations committed by states. The Fund may in its turn contribute to companies' complicity through its ownership. It is such complicity in a state's human rights violations which is to be assessed under this provision.

…

The acts or omissions must constitute an unacceptable risk of complicity on the part of the Fund. This means that it is not necessary to prove that such complicity will take place – the presence of an unacceptable risk suffices. The term unacceptable risk is not specifically defined in the preparatory work. NOU (Norwegian Official Report) 2003:22 states that "Criteria should therefore be established for determining the existence of an unacceptable ethical risk. These criteria can be based on the international instruments that also apply to the Fund's exercise of ownership interests. Only the most serious forms of violations of these standards should provide a basis for exclusion."[7] *In other words, the fact that a risk is deemed unacceptable is linked to the seriousness of the act. The term risk is associated with the degree of probability that unethical actions will take place in the future. The NOU states that "the objective is to decide whether the company in the future will represent an unacceptable ethical risk for the Petroleum Fund."* [8] *The word*ing *of Point 4.4. makes it clear that what is to be assessed is the likelihood of contributing to "present and future" acts or omissions. The Council accordingly assumes that actions or omissions that took place in the past will not, in themselves, provide a basis for exclusion of companies under this provision. However, earlier patterns of conduct might give some indications as to what will happen ahead. It is hence also relevant to examine companies' previous practice when future risk of complicity in violations is to be assessed.*

…

The following appears under the heading "Complicity and delimitation of companies' liability":

In order (for an investor) to be complicit in an action, the action must be possible to anticipate for the investor. There must be some form of systematic or causal relationship between the company's operations and the actions in which the investor does not wish to be complicit. Investments in the company cannot be regarded as complicity in actions which one could not possibly expect or be aware of or circumstances over which the company has no significant control."[9]

The above describes, first, the Fund's complicity. The company's unethical conduct must be expected by the investor. Moreover, there must be a link between the company's operations and the unethical actions. It is explicitly stated that circumstances beyond the company's control cannot entail complicity on the part of the investor. This must indirectly also be taken to mean that the company itself cannot be considered to be complicit in violations of norms that are beyond the company's control or which the company could not possibly expect or be aware of."

3.2 Complicity in human rights violations with regard to the relationship between states and companies

Complicity in an act may be taken to presuppose that another party is the main perpetrator. As already mentioned only states can in principle be held liable for human rights violations. It may consequently be asserted that a company's complicity can only be established in cases where it is determined that the main perpetrator of the same violations is a state. However, it is entirely possible under both Norwegian and international criminal law to sentence someone for complicity in an act without having established another party as the main perpetrator. The Council presumes that it was hardly the intention that the Council, as a precondition for establishing companies' complicity in human rights violations, should be required to determine whether states violate such rights. NOU 2003: 22 states:

"Since international law expresses a balancing of interests between states it is difficult to derive norms of action for market actors from sources of international law. On the other hand, international conventions give concrete form to the content of an international consensus on minimum requirements which should be imposed regarding respect for basic rights worldwide."[10]

In other words, international standards and norms can be indicative of which acts or omissions are deemed unacceptable, without asserting that companies are legally responsible for violations of international conventions. The Council accordingly assumes that the wording of Point 4.4.of the Ethical Guidelines does not require the Council to consider whether individual states violate human rights or labour rights standards each time it assesses a company's conduct in relation to this provision. It is sufficient to establish the presence of an unacceptable risk of companies acting in such a way as to entail serious or systematic breaches of internationally recognised minimum standards for the rights of individuals.

3.3 Wal-Mart's possible liability for violations of standards

The Council takes internationally recognised human rights conventions and labour rights conventions as its point of departure when assessing possible violations of standards on the part of Wal-Mart. Firstly, it must be assessed whether alleged violations of these standards take place and, secondly, whether they are serious or systematic. Furthermore, based on the Ethical Guidelines' preparatory work, the Council lists the following criteria which constitute decisive elements in an overall assessment of whether an unacceptable risk exists of the Fund contributing to human rights violations:[11]

- There must exist some kind of linkage between the company's operations and the existing violations of the Ethical Guidelines, which must be visible to the Fund.
- The violations must have been carried out with a view to serving the company's interests or to facilitate conditions for the company.
- The company must either have contributed actively, or had knowledge of, the violations, but without seeking to prevent them.
- The violations must either be ongoing, or there must exist an unacceptable risk that such violations will occur in the future. Earlier violations might indicate future patterns of conduct.

The specific acts and omissions of which Wal-Mart is accused will need to be considered in light of these criteria.

4 Wal-Mart's complicity in violations of standards

4.1 Alleged violations of standards at Wal-Mart's suppliers

4.1.1 Extent of the alleged violations

Wal-Mart has for some time been, and remains, the target of numerous campaigns directed at unacceptable working conditions at the company's suppliers. This involves both conditions falling far short of the standards Wal-Mart itself requires of its suppliers and complicity in violations of ILO labour standards and human rights standards.[12]

Violations of human rights standards among Wal-Mart's suppliers are alleged to take place in a large number of countries. The violations include employment of minors, working hour violations, wages below the legal minimum, health-hazardous working conditions, unreasonable punishment of employees, prohibition of unionisation and extended use of a production system that fosters working conditions bordering on forced labour.

4.1.2 Wal-Mart's supplier network

The company probably has the largest supplier network in the world. It has not been possible to determine the exact number of suppliers, but it clearly runs to tens of thousands worldwide.

In 2003, Wal-Mart imported goods valuing more than USD 15 billion from China, and is the world's largest individual importer from that country.[13] Wal-Mart's annual turnover is equivalent to about 2 % of the Gross Domestic Product of the USA, making it larger than the GDP of 161 of the world's states.[14]

In Wal-Mart's own report, "Factory Certification Report" for 2003–2004, the company states that it imports products from factories and suppliers in 70 countries.[15] The origin of the company's products is described as "tens of thousands of factories".[16] In 2004, the company claimed it had 5,300 suppliers with which it dealt directly. According to the company's annual report for 2004, *"We depend on over 68,000 suppliers"*.[17] This is assumed to include both domestic and international suppliers. Moreover, a single supplier can be assumed to have several factories, implying that the number of production sites is substantially higher than the number of suppliers.

Wal-Mart distinguishes between "*direct*" and "*indirect*" suppliers. A "direct" supplier is one that Wal-Mart deals with directly. The substance of the term "indirect" supplier is less clear. Wal-Mart states that the company also deals with indirect suppliers, and all

manufacturers within the so-called *"high-risk"* merchandise segments (footwear, garments, toys and sports equipment) are regarded as indirect suppliers.[18] *"High-risk"* signifies that the risk of unacceptable working conditions is regarded by Wal-Mart itself as greatest in these sectors.

4.1.3 Wal-Mart's monitoring regime

Wal-Mart operates a monitoring regime designed to ensure acceptable working conditions at 5,300 direct suppliers. The monitoring is said to encompass a further 2,300 indirect suppliers within the above-mentioned risk sectors.[19]

In 2004, Wal-Mart published a report giving the following information on conditions which the company itself describes as unacceptable.[20] Figures are stated as percentages of the 5,300 investigated suppliers:

Minimum wages and benefits not paid	46 %
Wage payments unverifiable	31 %
Violations of working hour provisions / working hours not registered	36 %
Seven-day working week	21 %
No documentation of employees' age	31 %
Unlawful employment contracts	10 %
No fire protection	35 %

It is not clear how inclusive this monitoring regime really is, given the fact that Wal-Mart itself reports that a *"(…) vast assortment of merchandise found in our stores is sourced from tens of thousands of factories in some 70 countries around the world."*[21] Nevertheless, it is safe to assume that the number of suppliers that are monitored is far lower than the total number of suppliers used by Wal-Mart.

A further question concerns the effectiveness of the monitoring regime in bringing to light unacceptable working conditions in the supply chain. A pertinent case in this connection concerns the dismissal of a Wal-Mart employee, *James W. Lynn,* who was responsible for auditing the company's suppliers in Latin America. Mr. Lynn claims he was dismissed because he truthfully reported on the working conditions at these suppliers. Wal-Mart denies that he was dismissed on this basis. Mr. Lynn has brought an action against Wal-Mart for wrongful dismissal.[22] Mr. Lynn explains in an interview how Wal-Mart planned its inspections with a view to revealing as few norm violations as possible.[23]

In the lawsuit *James W. Lynn vs. Wal-Mart stores Inc.*, it is stated that the company's inspection system, previously called the *"Factory Certification Program"*[24], was designed only to create the impression that working conditions at the suppliers are acceptable.[25] These claims accord with an earlier, extensive article in the magazine Business Week about working conditions at Wal-Mart's suppliers.[26]

A key objection to the company's monitoring regime is that inspections are generally announced well in advance, enabling the suppliers to temporarily improve orderliness and cleaning, construct false lists of hours worked, remove minors and coach employees in replying to questions if interviewed.[27] In 2003, Wal-Mart reported that 1 % of the inspections were carried out without prior notice. In 2004, this figure rose to 8 %, with the aim of raising it to 20 %.[28]

Another objection to Wal-Mart's monitoring regime is the absence of third-party verification. A majority of the inspections, 85 %, are conducted by Wal-Mart's own employees, the remainder by third-party inspectors approved by Wal-Mart.[29]

In James W. Lynn vs. Wal-Mart Stores Inc., the plaintiff contends that Wal-Mart's management exerts pressure on company employees who conduct inspections at suppliers to get them to modify the results. The plaintiff also claims that someone in Wal-Mart's local management in Honduras received bribes from factory owners in that country in order to have the factories approved as suppliers.[30]

A class action lawsuit has been brought against Wal-Mart, *Does vs. Wal-Mart Stores Inc.*, in which employees of Wal-Mart's suppliers in several countries hold the company responsible for unacceptable working conditions.[31] Wal-Mart is among other things alleged to have specific knowledge that a large number of its suppliers are acting in violation of the law and in violation of Wal-Mart's own guidelines.[32]

4.1.4 Wal-Mart's influence on working conditions within the supplier network

Wal-Mart's size gives it substantial market influence in the supplier industry. In fact, the company makes no secret of the fact that it imposes very stringent requirements on its suppliers to get them to cut their prices, enabling Wal-Mart to resell at low prices to the consumer.[33] Wal-Mart generally employs a tender arrangement involving a reverse auction whereby a number of suppliers are invited to deliver a particular item, and, after several rounds of competitive bidding, the supplier who bids the lowest price wins the contract.[34] Wal-Mart is also inclined to renegotiate agreements with its existing suppliers; earlier this year the company reportedly asked suppliers to cut their prices by 12 % to ensure contract renewal.[35]

Suppliers who are unable or unwilling to cut prices may find that Wal-Mart cancels the contract, preferring to find alternative suppliers elsewhere. In the case of suppliers who cut their prices, the result will in many cases be longer working days and pay reductions for employees, and a general worsening of working conditions. In connection with the investigation conducted for the Council, the manager of a supplier factory stated *"Wal-Mart is dominating buying and selling, therefore you have to match their demands … Big size and cheap price"*.[36] To the *Washington Post*, a representative of the Chinese labour authorities stated: *"Wal-Mart pressures the factory to cut its prices, and the factory responds with longer hours or lower pay… And the workers have no option."* [37]

Wal-Mart has introduced a system of production quotas which must be filled by suppliers. This system, along with the company's constant insistence on lower prices, forms the background for several of the violations of standards taking place in the supplier chain. A number of cases of working conditions bordering on forced labour have been documented, where employees are required to work very long days, seven days a week, without overtime compensation and without being allowed to leave the production site.

4.1.5 Examples of alleged norm violations by Wal-Mart's suppliers

Nicaragua[38] At the King Young S.A. factory, having Taiwanese owners, 80 % of the output is for Wal- Mart, above all Wal-Mart's apparel brand "Athletic Works".[39]

As is the case at a number of other production sites, there are reports of a system involving production quota requirements that are so stringent that employees invariably have

to work overtime in order to fill the quotas. Moreover, employees are reported to be locked inside the factory premises and subjected to various forms of abuse.[40]

Nicaraguan labour authorities have identified violations of working hour provisions, nonpayment for overtime and a number of violations of work environment and safety regulations. When the management learned that employees were in the process of unionising, the employees concerned were dismissed. More than 400 employees have been dismissed for this reason, in violation of national laws. Nicaraguan authorities have ordered the factory to reinstate the dismissed employees, to no avail.[41]

As regards Wal-Mart's inspections, Wal-Mart representatives are stated to have inspected the factory on several occasions, but there is no evidence that Wal-Mart has taken any action visà- vis the factory's management to address the poor working conditions.[42]

Working conditions at the K*ing Young S.A.* and *Presitex S.A.* factories are included in the grounds for the *class action Does vs. Wal-Mart Stores Inc.* These factories manufacture textiles for sale in Wal-Mart stores in the USA. It is alleged that employees at the factories are required to work overtime without adequate compensation and that wages are below the legal minimum. One of the plaintiffs also claims to have been dismissed because she tried to form a trade union.[43]

El Salvador *Hanchang Corporation of Korea* has factories in El Salvador, Sri Lanka, the Dominican Republic and in China. In El Salvador, the production for Wal-Mart takes place at the *Oriental Tex factory* which manufactures textiles under the brand names *Bobbie Brooks* and *Puritan*.[44] According to the information at hand, the most common type of norm violation at this factory is that employees are required to work 14–27 hours overtime per week without compensation.[45] The employees tell of threats, abuse and physical punishment and of a highly stressful physical work environment.[46]

Honduras When visiting Wal-Mart's suppliers in the Honduras, persons previously responsible for Wal-Mart's own inspections found a series of violations of wage and working hour provisions, padlocked fire escapes, poor physical work environment and various other conditions that were contrary to Wal-Mart's own Guidelines for suppliers.[47] The National Labor Committee has subsequently confirmed (by inspections conducted in April 2005) that these conditions have not been rectified.[48]

Lesotho There is information at hand regarding unacceptable working conditions at 21 of Wal-Mart's suppliers in Lesotho. They involve extensive use of unpaid overtime, low wages, various forms of physical maltreatment and harassment, a poor work environment and a ban on unionisation. There are also reports of a widespread practice of ordering employees to work on Sundays without this being registered or paid for, thereby ensuring that Wal-Mart's standard of one rest day per week is ostensibly observed.[49]

Kenya Oxfam International has reported similar conditions at suppliers in Kenya.[50] There are reports of very long working days with unpaid overtime, various forms of abuse and employees afraid to complain for fear of losing their jobs. The Council has also received information that employees at three factories in 2003 complained to the authorities over poor working conditions, long working days etc., and then went on strike. As a result, the factories were closed, only to reopen with a new workforce.[51]

Uganda Unacceptable working conditions have been brought to light at the Tri-Star factory in Uganda, in this case prompting a complaint to the ILO that the authorities are not enforcing work environment legislation or employees' right to strike.[52]

Namibia, Malawi, Madagascar
The main suppliers to Wal-Mart in these countries are Asian-owned textile factories. The Council is aware of a report dealing with working conditions at such factories in these countries. Here too there are consistent accounts of long working days, low wages, injuries due to lack of protective equipment and various forms of abuse and discrimination.[53]

Swaziland Information from several sources recounts unacceptable working conditions at Wal-Mart's suppliers in Swaziland.[54] In the class action *Does vs. Wal-Mart Stores Inc.,* working conditions at the textile factories *Leo Garments and Hong Yein* are included in the grounds for the lawsuit.[55] Both factories manufacture textiles for sale in Wal-Mart stores in the USA. It is alleged that the employees are required to work unpaid overtime and that wages are below the legal minimum.[56]

Bangladesh A report made for NBC Dateline using a hidden camera deals with working conditions at some of Wal-Mart's suppliers in Bangladesh.[57] The report, broadcasted on 17 June 2005, showed working conditions at a number of textile factories in Bangladesh. Consistently poor 10 working conditions with very long working days are shown, along with various forms of abuse and practices falling short of Wal-Mart's own requirements on its suppliers. The documentary also shows a production quota system requiring the employees to produce a specific number of garments per day, and that the employees cannot leave work until the quota is filled. There is no payment for overtime, and the report shows employees compelled to work from 8 am to 3 am the next morning, only to start work again at 8 am. Wal- Mart's comment on the report is said to be that the norm violations shown are commonplace: *"…the labor violations depicted on 'Dateline NBC' are common."*[58]

A report is also available from the National Labor Committee containing further documentation of working conditions at Wal-Mart's suppliers in Bangladesh. This alleges use of child labour (a 13 year-old girl) and the death of a young woman after working non-stop for 38 hours despite being ill.[59]

A further report describes how 6–7 employees at a textile factory outside Dhakar lost their lives and many were injured when the management called in the police after the employees had gone on strike. They went on strike because they were ordered to work five hours unpaid overtime per day, seven days a week. The police beat the employees with batons and opened fire with handguns. One of the injured in the shooting was a 13 year-old girl.[60]

Working conditions at Wal-Mart's suppliers in Bangladesh are described in the class action lawsuit *Does vs. Wal-Mart Stores Inc.,*[61] in which attention is drawn to conditions at the *Western Dresses and Lucid Garments* factories in Dhaka. Both these factories manufacture textiles for Wal-Mart's outlets in the USA. It is described how the factory management routinely engages private security forces, called *"Mastans"*, to terrorise employees who complain about working conditions or attempt to unionise: *"Mastans routinely assault, rape and in some cases kill workers who complain even about the most minute labor rights or who attempt to form trade unions."*[62]

China Wal-Mart is regarded as the largest individual importer of goods from China,[63] and 80 % of the production sites for so-called direct suppliers are Chinese.[64] There is, in addition, an unknown number of production sites for the indirect suppliers, possibly amounting to several thousand factories.

The Council bases itself on documentation in the form of a report[65] and film footage[66] on working conditions at a small number of Chinese factories.[67]

Supplier "X" supplies Wal-Mart from two factories in Guangdong. There are reports of very long working days, a seven-day working week, no guaranteed minimum wage, unpaid overtime and a system for providing false information at inspections. The latter includes manipulation of lists of hours worked, coaching and bribery of employees to give favourable answers to inspectors' questions, temporary change of accommodation to give the impression of less cramped conditions, and temporary removal of minors or illegal employees from the factory site.[68]

Supplier "Y" is a Korean company with factories in Guangdong that produce toys for Wal- Mart. Unlawfully long working days, no guaranteed minimum wage and production plans imposing unreasonable workloads on the employees are also reported at this supplier. However, inspections have brought to light some improvements evidenced by less manipulation of lists of hours worked and the like, and the employees are now paid somewhat higher wages.[69]

He Yi Electronics and Plastics Productions Factory (also operating under the name *Foreway Industrial China Ltd*.) manufactures toys for Wal-Mart and other companies. The factory has between 600 and 2,100 employees, depending on the season. There are reports of employees having to work 18–20 hour shifts, seven days a week, of wages below the legal minimum, of the absence of written contracts, and of a system for manipulating inspections. The Council's secretariat has received copies of checklists containing answers on working conditions that the employees are required to give at inspections, along with lists of hours worked showing 20 hour working days. The share of the factory's output going to Wal-Mart is said to be up to 20 %.[70]

In the class action *Does vs. Wal-Mart Stores Inc.*,[71] it is alleged that employees at two of Wal-Mart's suppliers in Shenzhen have been compelled to work without taking days off, holidays or rest breaks. The employer has withheld three months' wages to stop employees quitting. Moreover, mandatory overtime work has routinely been introduced without adequate compensation as well as health-hazardous working conditions.[72]

Indonesia Working conditions at some of Wal-Mart's suppliers in Indonesia are also described in Does vs. Wal-Mart Stores Inc. This involves the factories *PT Citra Bumilang Admitra and PT Busunaremaja Agracipta,* both of which manufacture textiles of the *"George"* brand for sale in Wal-Mart stores in the USA. It is alleged that employees are compelled to work unpaid overtime, that wages are below the legal minimum and, in general, that employees who seek to join a trade union are subject to violence, threats and harassment.[73]

4.2 Alleged violations in connection with the company's own operations

Allegations have been brought against the company for violation of labour law provisions at its operations in the USA and Canada. This refers, inter alia, to extensive use of

unpaid overtime, breach of rules governing the employment of minors, employment of illegal labour, extensive discrimination of female employees and measures to actively obstruct unionisation.

4.2.1 Discrimination of female employees

A number of civil lawsuits are pending against the company on a variety of grounds, among them Dukes vs. Wal-Mart Stores Inc., in which 1.6 million current and former female employees are bringing a class action lawsuit to seek compensation for discrimination.[74] A number of allegations are put forward against Wal-Mart, among them that the company discriminates against female employees in pay, training and promotion.[75] It is also reported that female employees who attempt to complain about such discrimination have lost their jobs.[76]

In *Dukes vs. Wal-Mart Stores Inc*., the plaintiffs base their case on alleged consistent discrimination of female employees in the company. This is supported by statistical analyses showing a pattern of discrimination in promotion and wages at Wal-Mart's operation in the USA.[77] According to the analyses, females have earned less than males in the same position, for virtually all positions, each year since 1996. The findings are confirmed in another analysis which similarly concludes that females are subject to a significant margin of wage discrimination, and that this cannot be put down to chance.[78]

A court ruling has been delivered permitting *Dukes vs. Wal-Mart Stores Inc.*, to be conducted as a class action. The federal judge[79] found that it is possible for a corporate culture that pervades an organisation to result in discrimination, although the company claims to counteract discrimination of its employees.[80]

4.2.2 Active obstruction of the employees' right to unionise

A spokesperson for Wal-Mart is quoted with the following statement about employees who wish to join a union: *"Our philosophy is that only an unhappy associate*[81] *would be interested in joining a union … so that's why Wal-Mart does everything it can to make sure that we're providing our associates what they want and need"*.[82] Officially, Wal-Mart has an *"open-door policy"* towards its employees, i.e. employees are free to raise questions and problems with the management. The company cites this as a reason why unionisation is not necessary.[83]

There is no employee unionisation at any of Wal-Mart's approximately 3,600 stores in the USA, and the same applies to Canada.[84] A complaint is reported to have been filed with the *US National Labor Relations Board* [85] against Wal-Mart[86] for breaking federal law by encouraging employees to inform against colleagues who wish to join a union. Another source *(Bloomberg)* has reported similar instances of the company actively seeking to identify and obstruct employees who wish to unionise.[87] A number of news media, including the *Wall Street Journal*, have also reported Wal-Mart's former vice-president Thomas M. Coughlin's so-called *"union project"* in which company funds were used to obstruct the formation of trade unions and to pay employees to pass on information about fellow employees who attempt to form such unions.[88]

Several of Wal-Mart's internal company documents, including a book entitled *"Wal-Mart: A Manager's Tool Box to Remaining Union Free,"* [89] are the object of a ruling by Canada's Supreme Court, in which the court ordered the company to surrender the book to the Labour authorities in Saskatchewan province.[90] The book refers to the company's managers as *"the first line of defence against unionization"*. The book also describes how managers should contact the company's "union hotline" if they suspect that employees

wish to unionise.[91] Wal- Mart has refused to turn over the book to the Canadian authorities referring to it as an internal document intended for use in the USA which has never been used in Canada.[92]

4.2.3 Violation of provisions concerning the employment of minors in the USA

Although it is not the worst forms of child labour that have been reported with respect to the company's operations in North America, there is information at hand on a number of violations of provisions governing the employment of minors.

In 2000, the company was fined[93] for violations of child employment provisions at all 20 Wal-Mart stores in the state of Maine.[94] In 2004, it was reported that Wal-Mart's own audit showed, after scrutiny of 128 stores, 1,371 instances of minors working too late in the evening, working in school hours or working too many hours per day. Earlier this year 2005, Wal-Mart decided to conclude a settlement in the lawsuit to avoid prosecution for violations of federal laws governing child employment in the states of Connecticut, New Hampshire and Arkansas.[95] The settlement encompassed 24 different instances in which employees under the age of 18 had operated dangerous implements and machines. As part of the settlement, Wal- Mart has undertaken not to employ persons under the age of 14 and not to allow employees under the age of 18 to operate cutting machines.[96]

4.2.4 Mandatory overtime without compensation

Wal-Mart is involved in a number of civil lawsuits in the USA. According to the *Wal-Mart Litigation Project,* the company currently faces 38 different lawsuits in 30 states.[97] A recurrent theme of the lawsuits is that the company systematically compels employees to work unpaid overtime. Wal-Mart is alleged to have withheld overtime payments to increase the company's earnings.[98] Moreover, a lawsuit against Wal-Mart in the state of Oregon is reported to have established that the company had coerced hundreds of local employees into working unpaid overtime, and that it did so after pressure by the company's central management.[99]

4.2.5 Use of illegal labour in the USA

It is reported that in 2003, the US authorities arrested 250 immigrants without valid residence permits who were working illegally in 60 Wal-Mart stores in 21 states in the USA.[100] These illegal immigrants, all of whom were engaged in cleaning, were chiefly employed by suppliers who apparently have also violated other laws and regulations governing work conditions.[101] In *Zavala, et al. vs. Wal-Mart Stores Inc.*, some of these immigrants brought action against Wal-Mart alleging that the company, together with its contractors, was *"engaged in and profited from a nationwide fraudulent scheme"*,[102] and that *"Wal-Mart is and was fully aware of and acted to aid and abet the rampant violations of federal and state law by the Contractor Defendants."*[103] The case ended in a settlement in March 2005 in which Wal-Mart agreed to pay USD 11 million.[104]

5 Other investors' exercise of active ownership

Several of the company's shareholders, in the first instance pension funds and other institutional investors, have for several years sought to achieve improvements in the company by exercising active ownership.

This has primarily been a matter of initiatives designed to improve Wal-Mart's monitoring regime in order to prevent norm violations within the company's own organisation and at suppliers.

In 2001, a coalition of 38 investors in the USA and Canada proposed that Wal-Mart should employ third-party inspections in its regime for monitoring suppliers. Interfaith Center on Corporate Responsibility (ICCR),[105] which coordinated the initiative, negotiated with Wal- Mart to get the company to try introducing independent, third-party inspections at one of its suppliers in Latin America. The initiative was unsuccessful since Wal-Mart concluded that the company's own monitoring regime was sufficient.[106]

In 2003, a group of investors proposed, at Wal-Mart's general meeting, that the company should introduce independent monitoring of its suppliers.[107] The proposal sought to: *"…commit the company to the full implementation of human rights standards by its international suppliers and in its own international production facilities, and to commit to a program of outside, independent monitoring of compliance with these standards."*[108]

In May 2005, the institutional investors F&C and USS, which together own about 11 million of the company's shares, wrote a letter to Wal-Mart expressing deep concern about *"the potential contingent liabilities and negative effects on the company's stock price and reputation"* in relation to the situation for employees in the company.[109] In 2005, the ICCR, on behalf of several investors, put forward a proposal for a resolution at the company's general meeting requiring Wal-Mart to prepare a report on what steps the company was taking too maintain employees' rights. The proposal states, among other things that *"… there has been no stated commitment for the company to develop a public sustainability report on its efforts to protect human rights, worker rights, land and the environment"*, and further, *"in the absence of open transparent public reporting, it is reasonable to conclude that the company has not addressed these issues adequately."*[110]

6 The Council's assessment

The Council is to assess whether there is an unacceptable risk of Wal-Mart acting in a way that may constitute complicity in serious or systematic violations of internationally recognised standards for human rights and labour rights. An assessment thus has to be made on whether the relevant acts or omissions by Wal-Mart fall within the scope of such norms or standards.

A distinction is drawn between violations of labour standards that take place at the company's suppliers, and violations within the company itself and vis-à-vis its own employees. The category first mentioned largely comprises violations taking place in parts of Latin America, Africa and Asia. The second category comprises violations of standards in the USA and Canada.

6.1 Violations of standards in the supplier chain

There is no doubt that working conditions at textile factories in Asia, Africa and Latin America can be abysmal, and that Wal-Mart purchases a number of products that are manufactured under unacceptable conditions. There are numerous reports of child labour, serious violations of working hour regulations, wages below the local minimum, health-hazardous working conditions, unreasonable punishment, prohibition of unionisation and extensive use of a production system that fosters working conditions bordering on forced labour, and of employees being locked into production premises etc. in Wal-Mart's supply chain.

All of the above examples represent violations of internationally recognised standards for labour rights and human rights.

All forms of harmful child labour are expressly forbidden. For example, Article 32 of the UN Convention on the Rights of the Child states that children shall be protected from performing *"any work that is likely to be hazardous or to interfere with the child's education or to be harmful to the child's health or physical, mental, spiritual, moral or social development."*[111] ILO Convention 182 on the Worst Forms of Child Labour, 1999, also explicitly prohibits all forms of harmful child labour.[112] Both these conventions enjoy broad international support. The UN Convention on the Rights of the Child has as many as 192 state parties, while the ILO Convention on the Worst Forms of Child Labour has 156. Both these conventions have been ratified by all the states mentioned in this recommendation, with the exception that USA has not ratified the UN Convention on the Rights of the Child. Since the standards prohibiting harmful child labour apply to the great majority of states, including the states mentioned in this recommendation, there exists, in the view of the Council, a risk that companies which avail themselves of such labour are contributing to serious human rights violations.

Circumstances that border on or constitute forced labour also constitute serious violations of fundamental standards. The International Covenant on Civil and Political Rights, Article 8 (3) states that *"No one shall be required to perform forced or compulsory labour."*[113] The same prohibition is enshrined in the ILO Conventions prohibiting forced labour.[114] Forcing persons to work beyond working hours without compensation may, depending on the circumstances, fall within the scope of the prohibition of forced labour.

Locking workers into production premises may also fall under the prohibition against forced labour. Such acts will in addition constitute a clear violation of the right to personal liberty. The International Covenant on Civil and Political Rights, Article 9, states: *"Everyone has the right to liberty and security of person. No one shall be subjected to arbitrary arrest or detention. No one shall be deprived of his liberty except on such grounds and in accordance with such procedure as are established by law."* Punishment and harassment are also violations of labour rights. Physical punishment in particular is a serious violation. The right to physical integrity and personal liberty are fundamental human rights and examples of international norms that lie clearly within what was categorised as *"an international consensus on minimum requirements regarding respect for basic rights worldwide" by the Graver Commission.* [115]

The violations mentioned here represent the most serious cases. It is recognised that violations of labour rights take place on a general basis in many states in the developing world. Point 4.4 of the Ethical Guidelines requires that the violations that may lead to exclusion must be serious or systematic and thus entails that not all violations of labour rights will be contrary to the Guidelines. The Council considers that the examples mentioned in this recommendation meet the criterion.

6.2 Violations of standards in Wal-Mart's own operations

It is relatively well documented that Wal-Mart pursues a consistent practice of gender discrimination, inter alia by pursuing a wage policy in which women and men receive different pay for the same position and work. The documentation in *Dukes vs. Wal-Mart stores Inc.*, appears to show that discrimination of women is widespread in the organisation. Such practice is contrary to both special and general human rights norms. The International Covenant on Civil and Political Rights[116] and the International Covenant on Economic, Social and Cultural Rights[117] contain explicit provisions (in Articles 2 and 3) that prohibit discriminatory differential treatment of women. The Convention on the Elimination of All Forms of Discrimination Against Women[118] further elaborates this pro-

hibition.[119] The same principle is established in ILO Convention No. 100, Equal Remuneration.[120] Since the USA is party to the International Covenant on Civil and Political Rights, there is, in the Council's view, a risk that the Fund may be complicit in possible violations of this Convention's standards regarding equal treatment of women and men.

It also appears to be well documented that the company puts a stop to any attempt by employees to form trade unions. Freedom to form trade unions and to join a trade union is a fundamental human right. This right is enshrined in a number of both general and special conventions. The two International Covenants from 1966 (on civil and political, and on economic, social and cultural rights) clearly establish that everyone has the right to freedom of organisation, association and assembly.[121] Article 8 of the Covenant on Economic, Social and Cultural Rights states that everyone has the right to *"form trade unions and join the trade union of his choice.."* Article 22 of the Covenant on Civil and Political Rights states *"Everyone shall have the right to freedom of association with others, including the right to form and join trade unions for the protection of his interests."* The right to organise is also enshrined in ILO Convention no. 87, Freedom of Association, 1948,[122] and in the ILO's Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy. Even so, US legislation do not always assure actual implementation of the right to organise, and there is therefore a risk of the Fund being complicit in potential violations of this right. Freedom of organisation is a fundamental democratic right, and clearly within the scope of what the preparatory work refers to as *fundamental rights.*

As stated above, Wal-Mart is regularly being accused of violating, in its own operations, rules preventing the employment of minors in dangerous work and at hours when minors are not supposed to work. The Council finds it probable that such practices may be widespread in the company. Moreover, documentation indicates that the company systematically compels employees to work unpaid overtime.

The Council assumes that the company, in a number of cases, has utilised illegal labour in its operations in North America. Several hundred violations of provisions concerning the employment of illegal immigrants can be cited. They do not appear to be a matter of isolated cases, but of repeated and wide-ranging violations of ethical norms. Where employees are working illegally, allegations of a dangerous work environment, unpaid overtime, wages below the legal minimum, prohibition of unionisation etc., are far less likely to emerge than would otherwise be the case. Illegal employees are at the mercy of the employer's terms and conditions. Hence there is reason to assume that the working conditions for illegal employees may be just as poor as the working conditions for legal employees.

6.3 The company's responsibility

With regard to the violations of labour standards taking place at the company's own production facilities and stores in North America, it is clear that the company is directly responsible. Where the alleged violations by Wal-Mart's suppliers are concerned, the responsibility is of a more derivative nature. It would be difficult to demonstrate direct responsibility for all norm violations taking place in the supply chain around the world. However, the Council's mandate is not to provide proof of events that have taken place earlier, but to consider whether an unacceptable risk exists that the company is complicit in, and will continue to be complicit in, violations of ethical norms.

The Council will, based on the documentation set out above, consider the risk of unacceptable violations of labour standards in relation to the four bullet points summarising

the preparatory work's criteria for establishing complicity in human rights violations, see above under section 3.3.

The first element in the assessment is whether there *exists some kind of linkage between the company's operations and the existing violations of the Guidelines which is visible to the Fund.* In the view of the Council, this is clearly the case. The violations of standards discussed above have taken place either in connection with the company's operations and activity in North America, or in connection with the manufacturing of goods for sale in Wal-Mart's stores. While it may be difficult to prove that Wal-Mart is directly responsible for violations of labour rights at its suppliers in the developing world, the Council considers there is an unacceptable risk that such a linkage exists. Where the violations of standards in the company's own business are concerned, the linkage between this business and the violations is relatively clear-cut. The linkage in this case is highly visible due to the keen public interest in Wal-Mart shown by the press and by a number of NGO's.

The second element in the assessment is whether the violations have been carried out with a *view to serving the company's interests, or to facilitate conditions for the company.* In the view of the Council, the type of violation focused on in this recommendation in Wal-Mart's business operations has been undertaken with the intention of increasing the company's profits. The Council considers that even though all companies aim at maximising their profits, it is ethically unacceptable to do so by committing, or tacitly accepting, serious and systematic violations of ethical norms. The Council finds that the violations have been undertaken with a view to facilitate or serving the company's interests.

The third element in the assessment is to consider whether the company has contributed actively to the violations, or has had knowledge of the violations, but without seeking to prevent them. Where the violations in North America are concerned, the Council considers that Wal-Mart is directly responsible for the reported violations, and must therefore be said to have actively contributed to them. Where the reported patterns of violations in the supply chain are concerned, the Council assumes that Wal-Mart is largely aware of them and largely refrains from seeking to prevent them. The Council also recognises that Wal-Mart wields substantial influence in regard to working environment, wages etc., particularly in relation to the manufacturers which the company itself describes as direct suppliers. This is due not least to the company's size and widespread presence in many countries, and thus to its engagement in a large number of suppliers.[123] In this respect too, the Council therefore considers that the company's acts and omissions fall within the scope of this element of the assessment. The fourth and final element in the assessment is whether the violations of standards are ongoing, or whether there exists an unacceptable risk that violations will occur in the future.

Here, earlier violations might indicate future patterns of conduct. The Council assumes that the patterns of action reported where Wal-Mart is concerned, are ongoing. To the Council's knowledge, there are no indications that the company plans to revise its approach in terms of seeking to prevent violations of labour rights at its suppliers, or as regards violations of standards for labour rights, including gender discrimination and prohibition of unionisation, within its own business operations. The Council has not received a reply to its enquiry to the company, nor do approaches from other investors appear to be prompting changes in the company's practices.[124] Hence in this case, it would seem that previous patterns of action may be an indication of future patterns of action. This implies, in the view of the Council, the presence of an unacceptable risk that serious and systematic violations of international standards are taking place today and may continue in the future.

The Council's point of departure is that the above four elements must *constitute decisive factors in an overall assessment*, and that it is not necessary that *all four* criteria be met in order for a company to be considered complicit in human rights violations. In the case at hand, however, all four elements together constitute an unacceptable risk of complicity in human rights violations.

As specified in point 4.4 of the Ethical Guidelines, violations of standards must be *serious* or *systematic* in order to provide a basis for the Council to recommend exclusion. It seems clear that a number of the violations reported, particularly in the supply chain, are very serious. They include violations of fundamental international standards with regard to child labour, working conditions bordering on forced labour, serious violations of work hour provisions, wages below the local legal minimum, health-hazardous working conditions, and unreasonable punishment. Isolated occurrences of this type, even if serious, would probably not suffice to exclude a company since such events would not constitute sufficient grounds for establishing a risk of violation in the future. In the case at hand, however, not seeking to avoid such violations by its suppliers seems to constitute a pattern of action on the company's part. Concerning violations of working environment standards, prohibition against unionisation and gender-based discrimination, these too will probably not be sufficient in themselves to recommend exclusion, even in cases where they must be regarded as systematic. In the view of the Council, what makes this case special is the total sum of violations of standards, both in the company's own business operations and in the supply chain. It appears to be a systematic and planned practice on the part of the company to operate on, or below, the threshold of what are accepted standards for the work environment. Many of the violations are serious, most appear to be systematic, and altogether they form a picture of a company whose overall activity displays a lack of willingness to countervail violations of standards in its business operations. Although it is legitimate to take steps to hold down prices on its merchandise and increase the company's profits, it is not legitimate to do so by violating applicable minimum standards. Since Wal-Mart is such a large company, this practice has consequences for a very large number of people both in many poor countries of the world and in North America.

Several investors have sought, through a variety of initiatives, to improve the company's practices in the areas addressed by this recommendation. Nothing suggests that Wal-Mart has complied with any of these initiatives, or that they have brought about improvements. Nor does the Council have reason to anticipate any movement by Wal-Mart to reduce the risk of the Fund's complicity in violations in the near future.

7 Recommendation

The Petroleum Fund's Council on Ethics accordingly considers that there is an unacceptable risk that the Fund, through its investments in Wal-Mart Stores Inc., and Wal-Mart de Mexico S.A., may be complicit in serious or systematic violations of human rights.

The Council recommends that Wal-Mart Stores Inc. and Wal-Mart de Mexico S.A. be excluded from the Petroleum Fund's portfolio.

Gro Nystuen	Andreas Føllesdal	Anne Lill Gade	Ola Mestad	Bjørn Østbø
(Chair)	(sign)	(sign)	(sign)	(sign)

Notes

1 http://www.hoovers.com/wal-mart-de-m %C3%A9xico/--ID__42411--/free-co-factsheet.xhtml
2 Wal-Mart Stores SEC Filing, http://investor.walmartstores.com/
3 Wal-Mart Stores Inc., "Factory Certification Report: March 2003 – February 2004," p 23. Entire report: www.walmartfacts.com/docs/131_NewsDeskFactShtSourcingarticle_1161280340.pdf
4 NOU 2003: 22, p 166.
5 The recommendation concerning Total S.A can be found in full at www.etikkradet.no.
6 NOU 2003: 22, p 34.
7 NOU 2003: 22, p 35.
8 NOU 2003: 22, p 35.
9 NOU 2003: 22, pp 164–165.
10 NOU 2003: 22, p 96.
11 Recommendation regarding Total SA, issued on 14 November 2005.
12 Wal-Mart Stores Inc. – Standards for Suppliers. Internal Code of Conduct. www.walmartstores.com/Files/SupplierStandards-Revisions12.2.04.pdf
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To The Ministry of Finance

Oslo, February 15, 2006
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Recommendation on exclusion of Freeport McMoRan Copper & Gold Inc.

Contents

1 Introduction

At a meeting held on 4 October 2005, the Council on Ethics for the *Norwegian Government Pension Fund – Global* decided to assess whether the investments in Freeport McMoRan Copper & Gold Inc.[1] may constitute a risk of the Fund contributing to severe environmental damage under the Guidelines, Point 4.4.

As of 31 December 2005 the Government Petroleum Fund, currently the *Norwegian Government Pension Fund – Global*, held shares worth NOK 116.3 million in the aforementioned company, the equivalent to an ownership interest of 0.174 per cent.

This is the Council's first recommendation on exclusion of a company on the grounds of contribution to severe environmental damage. In Chapter 2 of this recommendation, the Council interprets this concept, outlining the factors that will decide whether there is an unacceptable risk that the Fund may contribute to severe environmental damage.

In connection with its mining operations in Indonesia, Freeport has been accused of causing extensive damage to the natural environment. Freeport owns and operates one of the world's biggest copper mines in Papua, Indonesia, where it uses a natural river system for tailings disposal. Acid rock drainage from the company's overburden and waste rock dumps has also been reported. There is ample documentation that the company's activities have caused considerable and lasting damage to the riverine ecosystem, and that the company has taken very few steps to prevent or reduce such damage. These factors are described in further detail in Chapter 3.

In accordance with the Guidelines, point 4.5, the Council contacted Freeport through Norges Bank, requesting the company to comment on the abovementioned accusations. Norges Bank received a reply from the company on 20 January 2006. Freeport argues that the Council's presentation of its operations is inaccurate and based on outdated information and tendentious reports from anti-mining or politically motivated organisations. Freeport denies the allegations, but has not provided data or scientific evidence to support its claims that the mining does not cause severe and long-term environmental damage.

In order to establish whether there is a risk of complicity in severe environmental damage, a direct connection between the company's operations and the violations must be found. The Council assumes that the damage must be significant, emphasizing whether it leads to irreversible or lasting effects and whether it has a negative impact on human life and health. Furthermore, the extent to which the company's actions or neglect have caused the environmental damage must also be assessed, including whether the damage is a result of violations of national laws and international standards, and whether the company has failed to take adequate action in order to prevent or amend the damage. The likelihood of the company continuing its unacceptable practice in the future should also be taken into account. In the present case the Council considers that all these conditions have been met.

The Council concludes that the Ethical Guidelines, point 4.4, second paragraph, third bullet point provide a basis for determining that the Fund is currently contributing to severe environmental damage through its ownership in Freeport McMoRan Copper & Gold Inc., and does recommend exclusion of the company.

2 The Council's considerations

The Council shall assess whether the *Government Pension Fund – Global* can be said to contribute to unethical actions through its ownership interests in Freeport McMoRan Copper & Gold Inc.

2.1 The Council's mandate regarding severe environmental damage

The Ethical Guidelines, point 4.4, second clause, third alternative, states: "*The Council shall issue recommendations on the exclusion of one or several companies from the investment universe because of acts or omissions that constitute an unacceptable risk of the Fund contributing to: Severe environmental damage*."

The Council will consider the question of exclusion of Freeport according to this rule.

The remaining alternatives listed in point 4.4 concerning serious violations of individuals' rights in situations of war and conflict; serious or systematic human rights violations; gross corruption; or violations of other ethical norms may also be considered relevant in light of the serious allegations that have been raised against the company. The Council will briefly describe these accusations, but has chosen not to evaluate them with reference to breaches of the Ethical Guidelines as it deems that the company's contribution to severe environmental damage is sufficient to recommend exclusion.

2.2 On complicity and unacceptable risk

The Ethical Guidelines are based on the presumption that investors can be complicit in violations of ethical norms. Point 4.4 thus infers that the Fund may contribute to unethical acts through its ownership of shares in companies responsible for unethical acts or neglect.

Moreover, the company's acts or omissions must constitute an *unacceptable risk* of the Fund contributing to severe environmental damage (point 4.4). The preparatory work preceding the Guidelines does not explicitly define the term 'unacceptable risk', but states that: *"Criteria should be established for determining the existence of unacceptable risk. These criteria can be based on the international instruments that also apply to the Fund's exercise of ownership interests. Only the most serious forms of violations of these standards should provide a basis for exclusion."*[2] Hence, the unacceptability of the risk is linked to the seriousness of the act and how severe the environmental damage is.

The term 'risk' is associated with the probability of unethical actions occurring in the future. The basis for withdrawal is that the Fund must avoid placing itself in a position where it may contribute to an ethically unacceptable practice. The wording of point 4.4 makes it clear that the likelihood of contributing to present and future acts or omissions is the issue in question; hence, the Council assumes that actions or omissions which have taken place in the past will not normally provide a basis for exclusion under this provision. However, previous patterns of behaviour may give some indications as to what will happen in the future, and certain violations of ethical norms which have been initiated in the past could also be regarded as ongoing violations. This is particularly pertinent with regard to certain types of environmental damage where the result of previous acts or omissions continue to inflict serious harm on humans and the natural environment.

2.3 On severe environmental damage

The preparatory work[3] does not present a clear definition of the term 'severe environmental damage', indicating that it is not possible to determine with precision what the term encompasses, and that this must be assessed in each case: "*The Committee finds it*

reasonable that the exclusion mechanism is considered with regard to acts that cause considerable damage to the natural environment through pollution of air, water and soil; storage and disposal of waste; or interventions which have severe irreversible effects on the natural environment, for example in relation to biodiversity, protected areas or human health".

Environmental damage can be defined as a measurable adverse change in a natural resource or in the environment caused directly or indirectly by external agents. According to the preparatory work, this change must be considerable, and the damage must be directly linked to the company's acts or omissions. Consequently, the assessment of severe environmental damage must include the damage per se as well as the company's acts or omissions that have caused it.

2.3.1 Extent of damage

In assessing the extent of the damage, the following must be emphasized:

- the kind of environmental impact in question;
- the kind of damage caused by such impact; and
- the consequences of the environmental damage on the natural area's present and future qualities and on human living conditions.

Environmental impact

The preparatory work contains only limited considerations regarding the kind of environmental damage which qualifies for exclusion, but refers to various factors that may cause damage, such as air, water and soil pollution; waste disposal; and interventions in protected areas.

The Council accepts as a fact that pollution may include pollution associated with both the company's production and its products. The Council also regards waste management as a potential pollution problem, depending on how waste is handled, transported and treated.

Human intervention in natural areas can cause substantial environmental damage. According to NOU 2003:22, intervention in protected areas is a kind of environmental impact that can provide a basis for exclusion. To what extent intervention in protected areas constitutes severe environmental damage may, however, be difficult to assess, particularly if national authorities have revoked or given dispensation from the protection status of the area. Given that the Guidelines only recommend exclusion in cases of severe environmental damage, it is the Council's opinion that intervention in protected areas should not automatically qualify for exclusion, but be evaluated on a case-by-case basis.

A number of international conventions (with additional protocols) aim at protecting the natural environment or at limiting pollution and the dispersion of environmentally hazardous substances and waste from industrial production.[4] Such conventions reflect a global consensus regarding which environmental values should be protected and which pollutants should be limited or phased out due to their grave environmental or health impact. Even though the conventions are aimed at States, it is the Council's opinion that they provide a sound basis for deciding what kind of environmental impact related to companies' activities should be taken into account.

The Council's point of departure is that all types of pollution, intervention or exploitation of natural resources associated with individual companies' operations have the

potential to cause severe environmental damage. The impact may occur continuously over time or through accidents. The Council sees the environmental effects mentioned in the NOU 2003: 22 as examples and not as an exhaustive list.

Environmental damage

The environmental damage caused by emissions or interventions will depend on the kind and the extent of the impact or the intervention, as well as the receiving environment's vulnerability and resilience.[5] The harmful effects referred to in the preparatory work include damage caused by air, water and soil pollution, as well as severe irreversible impact on the natural environment, which for example afflicts human health and biodiversity.

Irreversible effects include the loss of species and natural areas (biodiversity), climate change, high concentrations of environmentally hazardous substances[6] and radioactive substances. Irreversible changes are serious due to their lasting consequences. The Council finds, however, that also other types of environmental damage can be regarded as severe, even though they are not necessarily irreversible in the strict sense of the word. Certain kinds of environmental damage resulting from extensive and prolonged contamination of water or soil may be gradually recovered if the pollution flow ceases. Nevertheless, the damage will generally persist over a long period of time, and a clean-up will require vast resources. Depending on the consequences, the Council is of the opinion that such damage may also be considered for exclusion.

Many pollutants released from manufacturing processes or product use have been proven harmful to human health. According to the NOU 2003: 22, serious damage to human health may provide grounds for exclusion. However, it is often difficult to *prove* that pollution from a particular company is harmful to public health. In such cases, the Council is of the opinion that it may be sufficient to establish such a correlation with a *high degree of probability*; however, an evaluation needs to be made on a case-by-case basis.

Consequences of environmental damage

The severity of environmental damage may be assessed in different ways, depending on the affected area's present or future functions, and whether economic, ecological, social or other values are given primary importance. Interventions in natural areas may often lead to the loss of ecological heritage for present and future generations. The question is whether this might be acceptable if the profits or social gains the intervention yields outweigh the benefits of preserving the area. Such gains must be measured against the actual loss of ecological value, taking into account whether endangered species or their habitats are adversely affected, whether the area contains unique values in terms of biodiversity, or whether it fulfils important ecological functions (water balance, protection against erosion, etc).

This assessment cannot be made on a general basis. However, the Council will emphasise that in order to regard loss of ecological value as severe environmental damage, the damage must be extensive, there must be degradation of special natural heritage features, or the damage must be of importance to future generations. The Council does not find it appropriate to establish general criteria for defining special ecological value or which consequences may be acceptable. Also this evaluation must be done on a case by case basis.

The Council considers that in addition to the loss of ecological value in itself, it must also be considered what consequences such a loss has for the people who are affected. In developing countries, for example, the natural areas may form the living areas and basis of

existence for many people, representing significant cultural or social values. Often when an area is damaged through physical intervention or pollution, the devastation does not only affect the local people's food and drinking water sources, but also their livelihood, identity, culture and traditions. The Council regards these aspects as pertinent to the evaluation of severe environmental damage.

When assessing severe environmental damage, the Council only includes damage of considerable proportions, and emphasizes, but does not limit its scope to, irreversible changes or significant negative effects on human life and health. Loss of ecological value and human habitat may constitute part of the criteria, and the probability of continued damage in the future must also be taken into account.

2.3.2 The company's acts or omissions

As for the company's practices, exclusion is only in question if the company is directly responsible for unacceptable violations of ethical norms. The NOU 2003:22 states that "exclusion should be limited to the most serious cases where the company in which the Petroleum Fund has invested is directly responsible for unacceptable breaches of standards, and there are no expectations that the practices will be discontinued."[7]

In other words, the company's acts or omissions must have caused the damage. Regarding the evaluation of the company's conduct, the preparatory work emphasizes two aspects: in which way the company's actions have produced the harmful effects, and what the company has done to avoid these.

According to NOU 2003:22, importance should be attached to the way in which the company's actions have caused the damage – "*whether the damage is a result of illegal actions, whether it is related to a systematic practice, whether it is planned, or whether it has escalated because of the company's attempts to conceal its actions*".[8]

Illegal actions may be understood as acts contrary to national laws and international treaties and norms. In a national context, illegal actions that cause serious damage to the natural environment will be defined as environmental crime[9], and according to the preparatory work, the exclusion mechanism is thus applicable.[10] If so, the Council assumes that only the most serious incidents of environmental crime should be considered, focusing on cases where the company has acted intentionally and it is probable that the practice will continue. If the practice is systematic, the requirements regarding the seriousness of the damage will be lowered.

International law, including international environmental agreements, does not place legal obligations on private companies, and companies can therefore not be accused of violating international law. However, several conventions set international standards for the protection of the natural environment and human life and health. In the environmental field, there are also international guidelines (for example within the EU) indicating best practice or best technology within different sectors with reference to pollution reduction, waste management, energy and resource use. Consequently, the Council regards international law and standards as normative also for companies' activities, especially in States with inadequate environmental legislation or ineffective enforcement, and where companies take advantage of this to avoid investing in environmental measures. The extent to which companies exploit weak environmental regulations in a country must, however, be evaluated on an individual basis. It is not necessarily reasonable to apply Norwegian or Western environmental standards in all situations. At the same time, lenient legisla-

tion in a country does not automatically justify a heavy environmental burden if the damage is considerable.

According to NOU 2003:22 it is relevant to consider environmental damage on the grounds of what can reasonably be expected from companies in terms of environmental responsibility – implicitly what companies have done to prevent and/or limit the damage. One such expectation "*is that companies have an environmental policy and management system designed to prevent severe environmental damage, both in the short and long term*"; furthermore, that "*companies do not take advantage of insufficient environmental regulation and lack of enforcement to lower their environmental performance in such a way that it leads to substantial damage.*"[11] The Council takes these observations as its point of departure for the following assessment. However, the evaluation of whether the measures adopted by a company should be regarded as sufficient, must be made on a case-by-case basis.

With regard to a company's acts and omissions, the Council infers that environmental damage must be judged as to whether the company has acted intentionally, whether the actions contradict international treaties and norms, and whether there has been a systematic failure to implement measures aimed at preventing or reducing the damage. This also implies an evaluation of whether it is likely that the practice will continue in the future and whether the damage will persist because the company has made no amends.

2.4 Summary

Based on the preparatory work for the Guidelines, the Council assumes that the Fund, through its ownership interests in companies, can be said to contribute to companies' complicity in severe environmental damage. The Guidelines are principally concerned with *existing* and *future* violations, although previous transgressions may give an indication of future conduct. At the core of the issue is the existence of an unacceptable risk that breaches will take place in the future.

Based on the preparatory work and the considerations laid out in section 2.3 above, the Council will make an overall assessment of whether there is an unacceptable risk that the Fund may contribute to severe environmental damage, emphasizing whether:

- The damage is significant.
- The damage causes irreversible or long-term effects.
- The damage has considerable negative consequences for human life and health.
- The damage is the result of violations of national law or international norms.
- The company has neglected to act in order to prevent damage.
- The company has not implemented adequate measures to rectify the damage.
- It is probable that the company's unacceptable practice will continue.

3 Freeport McMoRan Copper & Gold Inc.

Freeport McMoRan Copper & Gold Inc. is a mining company with headquarters in the USA. Through several subsidiaries it also has interests in energy production and copper refining.

The company is involved in mining operations only in Indonesia, where it owns and runs the Grasberg mine through a subsidiary, PT Freeport Indonesia. Freeport McMoRan has a 90.64 per cent stake in PT Freeport Indonesia, and the Indonesian state holds the remaining 9.36 per cent. In 1995, PT Freeport Indonesia formed a joint venture with Rio Tinto PLC, giving the latter a share of the profits from the Grasberg mine.

3.1 The allegations against the company

In relation to the mining activities in Indonesia, a number of environmental and human rights organisations, including Friends of the Earth Indonesia (Walhi), Jatam (Indonesia), the Mineral Policy Institute and Global Witness, have accused the company of extensive environmental devastation, abuses against the local population, complicity in human rights violations and corruption.[12]

The allegations concerning environmental devastation focus mainly on the company's use of natural river systems for tailings disposal, a practice internationally regarded as unacceptable due to its extensive and harmful effects on the environment. In December 2005 and January 2006 the company was accused of lacking a Government permission for riverine disposal. Moreover, the enormous waste rock and overburden stockpiles have been shown to generate acid rock drainage, and the company is criticized for not managing this satisfactorily. Allegedly, the environmental damage has also destroyed indigenous peoples' livelihood through the pollution of drinking water and a substantial reduction in hunting and fishing resources. Freeport is accused of not having compensated the local population sufficiently for the damage inflicted.

It is the company's complicity in severe environmental damage that forms the basis of the Council's recommendation.

The allegations concerning human rights violations are primarily connected to Freeport's cooperation with the Indonesian military, which have been hired as security forces for the company and have protected the mining area since the 1970s. For many years human rights organisations have reported on atrocities committed by the security forces against the local population, including killings, torture and abductions in and around Freeport's concession area.[13] Having been aware of the abuses, but doing little to prevent them, the company is accused of contributing to human rights violations that have taken place within its contract area. During the last year, several institutional investors have asked Freeport to account for its links to the Indonesian army, including payments made to the security forces.[14]

With regard to corruption claims, Freeport is said to have transferred substantial sums to named military officials. The paramilitary police forces, Brimob, have also been reported to receive large payments.[15] If this is the case, such practice is contrary to Indonesian law.[16] According to the company, US authorities have started making inquiries into the case since institutional investors requested the United States Securities and Exchange Commission[17] to investigate the accusations.[18] Freeport claims to have been open about its payments to the security forces.[19]
The Council has not examined in any further detail the allegations regarding complicity in human rights violations and corruption, but bases its recommendation on the environmental damage caused by the company's activities, which will be analysed below.

3.2 Background

The Grasberg mine is a huge mining complex located in the Indonesian province of Papua (earlier known as Irian Java) on the island of New Guinea.[20] Freeport's mining operation in Indonesia has been controversial ever since the contract was signed with the Indonesian Government in 1967. This is due to the fact that the activities have taken place in an area characterized by serious conflicts between the authorities and the local population, in which the company has been perceived to enjoy close ties

with the Indonesian Government (especially the Suharto regime) and the military, while its relationship with the local population has been marred by conflict.[21]

The prevailing view, particularly among Papua's indigenous population, is that the Government and the military[22] have taken resources and land from the people of Papua in an unlawful manner. Papua's natural resources (ore, forest and oil) are of great value to the Indonesian Government, the military and the business community.[23] The Indonesian state has given national and foreign companies concessions on land the Papuans regard as their own. Freeport is one example in this respect.[24] The extensive damage caused by the exploitation of natural resources that form the basis of existence for the majority of Papua's population reinforces the feeling of injustice. Moreover, the profits made by mining and the exploration of other natural resources have not benefited the society as a whole in any significant way. Weak environmental legislation and the Government's lack of enforcement have contributed to major environmental damage. Emissions from industry, and particularly mining, are among the main sources of water pollution on the island.[25]

The Grasberg mine

Freeport signed its first contract (a so-called Contract of Work) with the Indonesian government in 1967, acquiring exclusive mining rights within an area of 10 sq km in Ertsberg, which is part of the Grasberg complex. In 1988, the Grasberg copper and gold reserve was discovered, and production began in 1990. The contract was renewed for another 30 years in 1991, with the possibility of a 10-year extension. Grasberg has the world's largest gold reserve and the second biggest copper deposit. It is expected that the complex will be profitable until 2041, provided that additional mines are brought into production, among these a new opencast mine.[26]

The Grasberg mine is situated 4,000 m above sea level and borders on the Lorentz National Park, a UNESCO World Heritage site. Stretching from the mountains through the lowlands and down to the Arafura Sea, the area where the mining operations take place cover a distance of approximately 130 km in a region with extremely high precipitation (8,000–11,000 mm per year) and earthquake vulnerability.

The main extraction method is opencast mining, but there are also some underground mining zones. In 2004 about 640,000 tons of rock were mined daily, yielding approximately 185,000 tons of ore per day. The company expects to mine between 600,000 and 750,000 tons of rock per day until 2015,[27] generating a daily output of 240,000 tons of ore.[28] Overburden and waste rock will consequently amount to 360,000–510,000 tons each day. According to the licence, the company is allowed to process 300,000 tons of ore per day.[29]

The ore that contains gold, silver and copper is transported by conveyor belt to a flotation plant situated 1,000 meters lower than the mine. Here the ore is processed at a daily production rate of approximately 9,000 tons of copper concentrate.[30] The remainder, i.e. approximately 230,000 tons are tailings, which are disposed of. The concentrate is transported by pipeline to the port facility near Amamapare where it is dewatered and stored before being shipped.[31]

At the Grasberg mine Freeport has chosen to use a natural river system for tailings disposal, while overburden and waste rock are deposited in separate facilities. Until the scheduled closure of the opencast mine in 2015, Freeport estimates that a total of 3 billion tons of waste rock and overburden will be generated.[32] The cumulative production of tailings is estimated at 3.25 billion tons from start-up to 2041.[33]

Mining and the environment [34]

One of the main environmental challenges related to mining in general is the handling of large quantities of waste material. This also includes the Grasberg mine. Opencast mining starts with the opening of bedrock by removing vegetation and exploding rock mass to uncover the veins of ore. The so-called overburden is removed and stored for possible use once the mine has been closed. Gradually, the rock mass is dynamited and dug out into terrace-like structures. Generated waste consists of waste rock from the extraction and residues from the milling of the ore, so-called tailings. The tailings are a viscous mixture (slurry) made up of finely ground ore, process chemicals and water.

Because the ore metal content is relatively low, almost all extracted rock is deposited. The ore from the Grasberg mine has a copper content of 12 kg per ton, i.e. approximately 1 %.[35] This means that the amount of overburden, waste rock and tailings adds up to nearly 700,000 tons a day.

Riverine disposal

The disposal of tailings, overburden and/or waste rock in natural river systems is known as riverine disposal. Once the mine waste has been discharged into the water, the river transports it downstream to the flood plains where it is deposited (sedimented). The need for infrastructure is minimal, and if one disregards the environmental costs and possible reclamation, this is a very cheap method of waste disposal.

However, the practice causes major environmental damage as the riverine ecosystems are extremely vulnerable to the influx of large quantities of sediment. The sedimentation increases the danger of flooding, which contributes to raise the water level in the alluvial plains. As a result, the forests and vegetation along rivers and natural flood plains may die because the sediment reduces oxygen availability to the plants. In turn, this eradicates flora and fauna that cannot move to other areas, consequently influencing the availability of food to other species. As a rule, the water pollution increases considerably, not only due to sediment aggradation, but also because the tailings contain heavy metals and chemicals which are dissolved in the water. Besides being toxic to many aquatic organisms, these metals can also bioaccumulate. Depending on how polluted the water is, all aquatic life may die , the species composition may change, and the spawning areas for fish may be destroyed. In the sediments, the accumulation of metals can constitute a long-term pollution problem as the metals are released over time and thus become more accessible to living organisms.

To the population living from and along the river systems the effect is that the water is no longer fit for consumption. The hunting and fishing possibilities may be substantially reduced, influencing diets, nutrition and the traditional lifestyle. Flooding and changes in the river course can destroy crossings and make it difficult to use the rivers as transport routes.

Due to the severe environmental impact, riverine tailings disposal is prohibited in most countries, but Indonesia and Papua New Guinea still allow this practice.

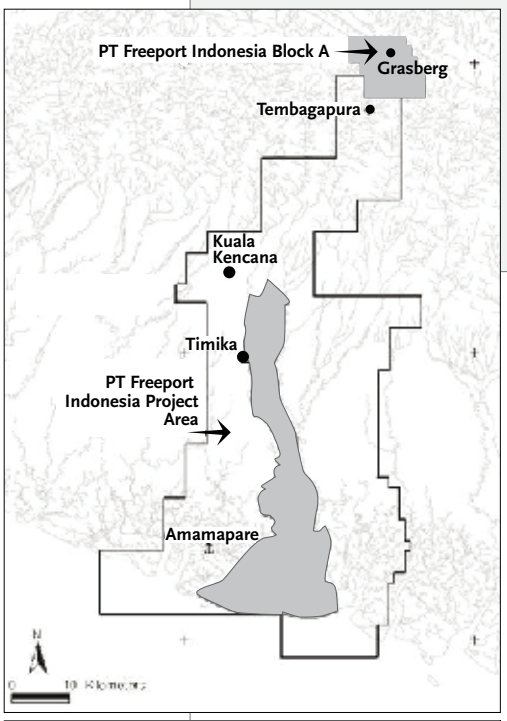
Acid rock drainage

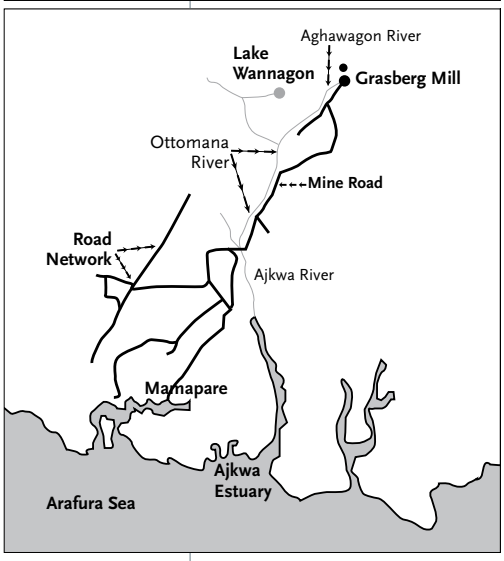
Acid rock drainage is a major issue associated with the disposal of waste rock and tailings. Worldwide, acid rock drainage is considered one of the most serious environmental problems related to mining.

Copper, gold, silver and other precious metals are often found in sulphurous rock. Acid rock drainage occurs when sulphide minerals come into contact with water and air (oxygen), producing sulphuric acid. In this process, heavy metals, which are found naturally in the ore, can be mobilised. The result is acid water containing heavy metals, which may cause considerable pollution of groundwater and river systems. Once initiated the process is irreversible and can continue for hundreds of years.

Ore characteristics, temperature and rainfall, among others, will influence acid rock drainage. The duration of the process is crucial in terms of environmental damage, as it may imply a more or less continuous release of heavy metals over a great number of years and with devastating effects on river systems and groundwater. In practice, this could eradicate all life in a river system for a very long time, making reclamation a difficult and extremely expensive process.

Figure 1:
The Grasberg area[38]





Measures aimed at mitigating acid rock drainage depend on whether the mine is in operation or has been closed down. Mixing or adding minerals that can neutralise the acid, covering rock mass and deposit sites with geomembrane and/or compacted clay soil are among such procedures. The results will vary according to the containment method and the natural conditions of the site.

3.3 Environmental damage

3.3.1 Tailings disposal

Freeport uses a natural river system to transport the tailings from the mountains to the socalled Modified Ajkwa Deposition Area. Every day nearly 230,000 tons of tailings are tipped directly into the Aghawagon River, an affluent to the Otomona River. The Otomona runs through a plain covered by rain forest before flowing into the Ajkwa Estuary [36] (see figure 1). The greater part of the tailings is deposited on the flood plain, while the remainder reaches the estuary where it is poured into the Arafura Sea, being carried up and down the coast by tidal waters and ocean currents.

The choice of riverine disposal as a waste management method was based on a daily output of 7,500 tons of ore. Today the production and, consequently, the discharges are more than 30 times bigger.[37] The environmental impact is associated with the large amount of sediment and hazardous substances that are being fed into the river system.

Sediment input

Tailings discharge produce large sediment loads on the riverbed. According to information obtained by the Council, Freeport's own reports for the second quarter of 2005 show a suspended solids[39] concentration of 732,000 mg/l at the point of discharge upstream of the deposition area and 1,300 mg/l downstream of the area.[40] Tests performed by the environmental authorities in 2004 show a concentration

of 37,500 mg/l at the point where the river reaches the lowlands, and 7,500 mg/l where it flows into the Arafura Sea.[41] Indonesian standards establish a maximum limit of 400 mg/l.[42] The input constitutes a considerable transgression of these standards.

The Modified Ajkwa Deposition Area occupies 235 square km[43] and is enclosed by levees to the east and the west, but is open both downstream and upstream. Located on each side of the river, the levees are 3 km apart and 40 km long.[44] The layers of tailings deposited between the levees are expected to attain a thickness of 10–15 m.[45]

As the deposit site is being filled with sediment, an increasing amount of tailings will also reach the coast. Freeport's 1997 environmental impact assessment estimates that 37 per cent of the tailings have flowed into the ocean and that this portion may rise to 50 per cent. [46] New York Times reports that around one third of the waste has reached the estuary.[47] Other sources estimate that the emissions to the river delta and the sea will escalate to 76,000 tons per day as the deposition area fills up.[48] In its reply to the Council, Freeport states that only 14 per cent of tailings seep out of the deposition area, and that a part of this runs through the mouth of the Ajkwa River into the Arafura Sea.[49] Freeport also informs that the company has adopted measures in the deposition area that it believes will contain a larger part of the tailings.[50] Even if the estimates vary significantly, there is no doubt that the estuary and the coastal zone are affected by the discharges. Freeport argues that Indonesian authorities know and have accepted that a part of the tailings escapes the deposition area.

According to Freeport's own environmental risk assessment, model estimates indicate that the ocean currents will disperse tailings along the coast to the estuaries on the eastern and western sides of the Ajkwa River mouth, something which visual observations can confirm.[51] Nevertheless, in its response to the Council, Freeport claims that its monitoring programmes do not show any sign of long-term adverse environmental effects in the Arafura Sea.[52]

Hazardous substances in the tailings

In addition to the physical effects of the enormous quantities of waste that are dumped daily into the river, the content of environmentally hazardous substances also has a bearing on the damage. The tailings discharge contains heavy metals and processing chemicals.[53]

According to the company itself, the tailings include heavy metals such as copper, arsenic, cadmium and mercury.[54] Among these, copper is the substance found in the largest quantities. Copper is acutely toxic to aquatic organisms, including invertebrates, fish and amphibians.[55] It can also cause long-term adverse effects on the environment. The copper concentration seriously affects aquatic organisms' reproduction and chances of survival. In this context it is highly probable that copper is the most crucial metal with regard to water quality.[56]

Freeport argues that the water quality in the river is good and that the company meets Indonesian drinking water standards for dissolved copper.[57] In its reply to the Council the company points out that its surveys show dissolved copper concentrations well below the official requirements and that the copper content in tailings does not pose any health or environmental risks.[58] Yet, these claims are not substantiated with any concrete data.

Furthermore, the company declares that analyses carried out inside the Contract of Work area do not register significant levels of mercury in tailings, water or sediments; nor have any appreciable residues of processing chemicals been detected.[59] However, these statements are not documented any further.

Environmental organisations have raised considerable doubts concerning Freeport's assertions and monitoring results. In 1994, the US government agency *Overseas Private Investment Corporation* (OPIC)[60] performed a detailed review of the mining operation.[61] The study refers to Freeport's environmental risk assessment of 1994, which states that copper discharge in tailings amounts to approximately 0.15 per cent (the equivalent of 1,500 mg/l). These figures indicate a massive copper load entering the riverine and marine ecosystem, something which according to OPIC's assessment most probably will cause severe irreversible effects.[62]

Freeport's own reports to the Indonesian Ministry of the Environment for the second quarter of 2005 show copper levels of 0.022 mg/l downstream of the deposition area[63]. At the same time, other samples taken by the Indonesian Ministry of the Environment just outside the deposit site reveal that copper levels often exceed 0.03 mg/l.[64] In the areas around the river mouth, high copper concentrations in water and sediments were also confirmed through Freeport's risk assessment, reaching levels that may be acutely toxic to aquatic organisms.[65] In its reply to the Council, Freeport claims that its tests do not indicate high pollution levels in the water, but no further evidence is provided to support the assertion.[66]

The Council has refrained from any detailed analysis as to why the test results differ. Irrespective of the method used, the sampling indicates a considerable supply of copper into the environment. Compared to both Australian and American water quality standards, the copper concentration exceeds the limits for what is considered toxic to aquatic organisms.[67] Copper also has a bioaccumulation potential in sediments and organisms.[68] As early as 1994, OPIC's evaluation strongly criticized the fact that the effects and consequences of high copper discharge levels had not been examined.[69] The criticism has since been repeated several times by environmental organisations. In its reply to the Council, Freeport refers to the environmental risk assessment, claiming that copper content in tailings does not pose any form of environmental or health threat.[70]

Environmental damage

The OPIC review concluded that Freeport's tailings management had caused substantial adverse environmental impact on the Ajkwa and Minajerwi Rivers, and that the mining operation continued to represent unreasonable or major environmental, health or safety hazards with respect to the river systems affected by tailings, the surrounding terrestrial ecosystems and the local inhabitants.[71] As a result, OPIC revoked the insurance policy for the Grasberg mine in October 1995, but after intense lobbying from American politicians who supported Freeport, it was temporarily reinstated from April 1996 until the end of that year.[72] Later in 1996, Freeport itself chose to terminate the contract.[73] Based on the investigations the Council has undertaken, there is little to suggest that the company's environmental record has improved since OPIC conducted its review.

According to an internal memorandum from the Indonesian Ministry of the Environment in 2000, the riverine disposal has destroyed all life in the river systems.[74] The environmental risk assessment commissioned by Freeport and Rio Tinto in 2002 also makes it clear that the river systems between the point of discharge and the deposition area, as well as

the areas inundated by tailings, are unfit for aquatic life.[75] The rivers running through the lowlands that constitute the deposition area have been described as one of the most biodiverse habitats in the world.[76] This ecosystem is now completely destroyed.

In its reply to the Council, Freeport refutes the accusation without providing any further details. Instead Freeport points out that riverine disposal is the best alternative, given the extreme topography of the area, the heavy rainfalls and the danger of earthquakes, which increase the risk of landslides if the waste material should be deposited on land. The company claims to be cooperating with national and international experts "*to ensure that the tailings management practices represent the best possible alternative.*"[77] Freeport regards its mining operation as environmentally responsible, maintaining that the water quality in the river satisfies Indonesian and American drinking water standards for dissolved metals.[78]

The tailings disposal also causes extensive flooding, a phenomenon that has destroyed large parts of the nearby riverine rainforest. Around 2000, it was reported that in an area covering 30 sq km, the riverine rainforest and other vegetation (including sago, which is an important food crop for the local population) had died.[79] This was confirmed in a study from 2001, conducted by the Indonesian environmental organisation, Walhi, in cooperation with the *National Space and Aeronautic Institute* (LAPAN). Satellite pictures showed that more than 35 sq km of lowland forest and 84 sq km of the Arafura Sea were adversely affected by the discharges.[80] The vegetation is smothered by oxygen starvation because the sediment load reduces oxygen availability. According to information obtained by the Council, the area of devastation has expanded further during the past 5 years as a result of Freeport's production increase and failure to adopt measures to reduce the discharges.[81] By the time the mine is closed down, it is expected that the dead vegetation zone will include all 230 sq km of the deposition area.[82] According to Freeport, another 220 sq km will be affected by the tailings outside the deposition area.[83] The implications of this are not explained. When forests and other vegetation die back in such a huge area, there will be significant consequences for the whole terrestrial ecosystem, including animal life.

Freeport does not deny that this damage has occurred, but refers to the Government permit for the deposition site. In its reply to the Council, Freeport states that the authorities are aware of the observed environmental damage and that the authorisations the company has received to increase production are tantamount to the Government's acceptance of this damage.[84] The company denies that the damage is severe or irreversible, alleging that it plans to reclaim the whole deposition area once the mining operation is concluded.[85] According to Freeport, extensive research and successful trials have been conducted to cultivate the affected areas, both in the mountains and in the wetlands. As soon as the mining operation has come to an end, the company's goal is to convert the whole deposition area into productive farmland or natural areas with native vegetation.[86] Freeport also claims that tests show how native species regenerate naturally in soil containing tailings.

In 2004, slightly more than 0.06 sq km of the deposition area's 230 sq km was reclaimed.[87] Freeport has not given any concrete details regarding its yearly goals for the rehabilitation of these areas. Even if Freeport does not offer any detailed information, the demonstration trials seem to largely have taken place on the very outskirts of the deposit site (outside the levees) where tailings form a relatively thin layer and the soil has been enriched with considerable quantities of compost. To the Council's knowledge, Freeport has not mentioned anything about the likely success rate of reclamation with sediments deeper than 10 metres.[88] On the basis of information provided by Freeport and given the actual

dimensions of the deposition area, the Council regards it as rather improbable that the environmental damage caused by the operation will be significantly reduced through the reclamation plans presented by the company.

The estuary where the Ajkwa River runs out into the Arafura Sea has also been affected since parts of the discharge seep out of the deposition area. According to Freeport's environmental risk assessment, the species composition and the supply of fish and invertebrates have changed significantly, meaning that for example organisms which depend on clear waters do no longer exist in the affected areas of the estuary, and that the biodiversity has been substantially reduced. [89] In other words, the estuary has lost ecologically important species and these have been substituted by organisms adaptable to polluted water.

In its reply to the Council, Freeport claims that the estuary (situated below the actual deposition area) is a functioning ecosystem.[90] In light of the factors mentioned above, the assertion might be correct, but in this context it may nevertheless be perceived as misleading. Freeport does not provide any information as to the fact that the estuarine ecology has changed significantly over time; neither does the company mention anything about the long-term impact of the continuing sediment input. With regard to the Arafura Sea, Freeport claims its tests show that the water quality meets relevant standards, but does not specify this any further. As a matter of fact, the company informs that there has been a slight reduction in the species composition among organisms which live on the seabed adjoining the river outlet,[91] but it does not elaborate on the consequences.

Social impact

There are 71 villages in the mining area (Mimika district), of which 29 are strongly influenced by the operation.[92] The Amungme (mountain people) and the Kamoro (lowland people) are indigenous peoples who live in the areas affected by the mining. Their livelihood used to be based on subsistence farming, hunting, fishing, and gathering of sago and other forest produce. The river was their main source of drinking water and was also used for washing, bathing, etc. Their culture and identity are entwined with and based on the surrounding landscape. Riverine disposal has had the biggest impact on the inhabitants of the lowlands, whereas the mountain people have been more affected by the actual mining.

Frequently there have been reports on conflicts with and violations against local inhabitants. Freeport is accused of lacking respect for the indigenous people's culture and traditions, destroying the livelihood of people in the area, and not compensating them for their losses.[93] Through the Contract of Work, Freeport was given powers to take land, timber and other natural resources, and to forcefully relocate the inhabitants to new areas.[94] This dislocation has occurred with help from the Government and the use of security forces.[95] A number of reports show how the mining and the adverse effects of riverine disposal (see above) have destroyed the livelihoods and the cultural values of the area's inhabitants.[96] Similarly, the OPIC evaluation has pointed out the major and unreasonable damage inflicted on humans and the natural environment as a result of Freeport's tailings management.[97]

Freeport has paid compensation, but the local population claims that this does not cover the loss of natural heritage features such as clean water, farmland, hunting and fishing grounds, and other losses of natural and cultural values.[98] Freeport refutes such allegations, arguing that the company through its social and economic development program-

mes cares for the local communities' interests and that it has contributed to improving their living standards.[99] In 2000, after five years of negotiations, the company signed a "*memorandum of understanding*" with Amungme and Kamoro organisations as well as local authorities, focusing on socio-economic resources, land rights and environmental issues.[100] The company has created a separate fund for the Amungme and Kamoro. In 2004, USD 6.5 million was allocated to the fund, and the company has scheduled yearly transfers of USD 1 million. This fund is an addition to the so-called *Freeport Partnership Fund for Community Development*, which was established in 1996 and currently stands at USD152 million. The money is spent on school projects, education, hospitals, health services, social and business development for the local population, etc. [101] According to information received by the Council, the management and distribution of the fund have been subject to criticism for creating serious internal conflicts between local communities.[102]

3.3.2 Disposal of overburden and waste rock

Overburden and waste rock are being disposed of in two valleys that border on the mine and contain four stockpiles – *West Grasberg*, *Wanagon*, *Lower Wanagon* and *Carstenz*. The waste volume amounts to 360,000–510,000 tons per day.[103] As mentioned earlier, according to current plans the deposits of waste rock will total some 3 billion tons during the mine's lifespan.[104] Being up to 300 m deep in certain places, the stockpiles now cover an area of approximately 8 sq km.[105]

In 1993, acid rock drainage from the stockpiles was observed for the first time.[106] There have also been reports of ongoing seepage into the groundwater [107] which, among other things, has resulted in the contamination of springs in the Lorentz National Park.[108]

Freeport acknowledges that acid rock drainage has occurred and that there is a risk of continued run-off from the stockpiles.[109] The company asserts that it has implemented measures expected to reduce future acid rock drainage and that the necessary steps will be taken in this regard.[110] In its reply to the Council Freeport states:[111]

- *"Freeport has extensively studied the potential for production of ARD[112] and is managing its overburden stockpile plan to take these potentials into account."*
- *"[Freeport] has designed an ARD collection and treatment facility and continues to monitor and upgrade modelling of groundwater flows in the area to assist in addressing ARD issues."*
- *"A major aspect of the studies' focus has been to determine best procedures for overburden stockpile closure. These procedures both prevent and, where required, mitigate any ARD generation."*
- *"Acid rock drainage mitigation plans provide for capture and treatment of the existing acid rock drainage, in conjunction with limestone blending and limestone capping of existing overburden placement areas to minimize future acid rock drainage generation."*
- *"In addition, PT-FI[113] has an established response plan [*to acid-generating tailings*] that includes, among other things, the application of lime or limestone to neutralize any indication of acid-producing potential within the tailings deposition area."*

However, Freeport does not give any further details as to when and how the plans will be carried out, or what this actually implies; for example, which tests are being conducted, which parameters are being monitored, and how acid rock drainage is expected to develop in the future. The Council considers the information presented by the company to be general and observes that the company chooses not to support its assertions with concrete data and scientific evidence.

3.3.3 Violation of national law

In an article about Freeport published in the New York Times on 27 December 2005, allegations were made that Freeport does not possess any permission for riverine disposal and that the pollution levels in the discharges do not meet Indonesian standards. The article also revealed that since 1997 the Indonesian Ministry of the Environment has repeatedly warned the company of its violations of the law and recommended it to stop the riverine disposal.

In 1999 the Government revised the legislation regarding hazardous waste, classifying tailings as environmentally harmful. Based on testing of the tailings, the authorities may deviate from this. However, the Government does not consider Freeport as exempt from the rule, stating that the necessary discharge permit has not been issued.[114] In January 2006 the Minister of the Environment appointed an investigative commission to evaluate the extent of the environmental damage.[115]

In its reply to the Council, Freeport claims to operate in accordance with the requirements and orders issued by Indonesian authorities, denying any irregularity: "*The new regulations stated that mine tailings can be classed as "non-hazardous" if certain tests are conducted and standards are met. Over the years, PT-FI has submitted the results of extensive test work showing that tailings are non-toxic based on United States, Australian and international protocols*". [116] The company points out that it has received other licences, for example through the Government approval of its risk assessment (300K AMDAL) and the permission from Papua's Governor to use the rivers for waste disposal. Freeport does not inform whether it explicitly has applied for a new discharge permit under the revised law.

The local Governor, however, does not have the authority to issue such permissions. This is confirmed through a letter from the Indonesian Minister of the Environment to the Governor of Papua and other officials written in 2001. The letter states that the licence is invalid and the Governor is asked to revoke the permission given to the company.[117]

The Council believes that Freeport has been aware of the Ministry's opinion in this case. At the same time, it seems as if the authorities' failure to enforce environmental regulations has, in part, made the company consider it unnecessary to clarify which requirements should be complied with.

4 The Council's assessment

4.1 Freeport's reply to the Council

The Council, through Norges Bank, sent its report to Freeport on 22 December 2005, requesting a reply within 3 weeks of receipt. On 20 January 2006, Norges Bank received the company's reply.

In its response, Freeport states that *"the portrayal of FCX [Freeport] is utterly false and bears no resemblance to our company and its operations. This is perhaps because the report appears to be based largely on outdated information or biased reports issued by non-governmental organizations who are anti-mining or have a political agenda."*[118] The company's comments regarding each item are discussed above and also in the present and following sections.

Even though Freeport's reply is comprehensive, the Council does not see it as providing much new information. Freeport denies the accusations made against the company, but chooses not to present data, test results or other concrete information or scientific evidence

which might substantiate its claims that the mining operation does not cause severe and lasting environmental damage. The Council observes that Freeport's response to many issues raised in the report is vague and hardly to the point with regard to the problems at hand.

The Council would like to emphasize that Freeport has been given the opportunity to present any information it may wish and thus substantiate its assertions. Nevertheless, Freeport has not provided any concrete data. In its letter to the Council, the company refers to a series of environmental studies it has conducted, claiming that these are available from the Indonesian authorities. However, Freeport decides not to present them to the Council. This is also the case with the test results from the environmental monitoring programmes. In the Council's view, this lack of transparency and concrete information renders it impossible to verify the company's assertions, thus making them lose credibility.

4.2 The Council's assessment regarding risk of contribution to severe environmental damage

The Council's task is to assess whether there is an unacceptable risk that the Fund through its ownership in Freeport may contribute to severe environmental damage, as stated in the Guidelines point 4.4, second paragraph, third bullet point, and in accordance with the interpretation presented in Chapter 2 above.

It is a fact that the mining operation owned and run by Freeport has caused the environmental damage described in Chapter 3 of this recommendation. On the basis of the above-mentioned documentation, the Council will evaluate whether the environmental damage provoked by the company is serious enough to constitute a violation of the Guidelines. This assessment is linked to the summary in section 2.4.

The first aspect to be assessed is the *scope of the damage and to which extent it leads to irreversible effects*. There is no doubt that riverine tailings disposal represents the overriding environmental problem of Freeport's operations today. In the Council's view, the daily disposal of 230,000 tons of tailings generates severe and long-term environmental damage, as described in section 3.3.1. Furthermore, the Council deems it probable that acid rock drainage from the stockpiles will constitute an increasing and considerable environmental problem with potentially far-reaching harmful effects in the future, as shown in section 3.3.2. Consequently, the Council assumes that the damage is severe and that there is an unacceptable risk that the environmental impact caused by the mining operation is lasting and irreversible.

The Council also regards as unacceptable the risk that the environmental damage may have adversely affected *human life and health*, as described in section 3.3.1 (Social Impact), even if this issue has not been treated as thoroughly as the physical impact.

The next question is whether the company's conduct is contrary to *national law and international norms*. Freeport claims, for example in its reply to the Council,[119] that the company complies with all national environmental regulations. However, the Council has found that Indonesian authorities question whether the company has a valid permission for riverine disposal at all and whether the water quality standards are met, see section 3.3.3. In this context it may be relevant to point out that the environmental standards required by Indonesian authorities fall significantly short of current rules in the company's country of origin, the USA, where riverine disposal is prohibited.

The Government has not enforced its environmental regulations to much effect. This means that the consequences of not meeting the standards are of little significance to the company. Weak environmental legislation and lenient enforcement indicate that there is no system in place to reduce the damage caused by mining, something which contributes to further aggravating the risk of severe environmental damage.

There are no international conventions or guidelines regarding best practices for waste disposal in the mining industry,.Currently, the EU is preparing a directive on waste management from extractive industries which will lay down comprehensive European requirements.[120] To the Council's knowledge, Indonesia and Papua New Guinea are the only countries that still allow riverine disposal.

The World Bank no longer finances projects which make use of riverine disposal, and the International Finance Corporation does not accept the procedure unless specific discharge limits are complied with. In practice these limits mean that the discharge must be treated before it is released into river system.[121]

"The Extractive Industries Review" (EIR) from 2003[122] and the international project *"Mining, Minerals and Sustainable Development"* (MMSD)[123] also advise against riverine disposal owing to the environmental damage involved. EIR states: *"Scientific evidence clearly demonstrates that this method of waste disposal causes severe damage to water bodies and surrounding environments... In practice, this technology is being phased out due to recognition of its negative consequences: today only three mines in the world, all on the island of New Guinea, still use this method to dispose of mine wastes. The EIR agrees with the call for a ban on riverine tailings disposal."*[124] In its recommendations regarding best practices for the mining industry, MMSD calls for *"a clear commitment by industry and governments to avoid this [riverine tailings disposal] practice in any future projects"* as this *"would set a standard that would begin to penetrate to the smaller companies and remoter regions where this is still accepted practice."*[125] The world's largest mining company, BHP Billiton, has also declared that it will not make use of riverine disposal in its new projects.[126]

The Council places great importance on the fact that key international players and the authorities in many countries consider riverine tailings disposal to be an unacceptable waste management method due to its harmful environmental effects. On these grounds, the Council judges Freeport's practice as clearly in breach of accepted international norms. The Council also believes that Freeport through this conduct is taking advantage of the low environmental standards and the lenient law enforcement in the country where it operates.

Moreover, the Council must reach a conclusion as to whether the *company has failed to take action aimed at preventing damage, including whether the omission was planned.*

Riverine disposal has been a conscious choice on Freeport's part, and repeatedly, also in its reply to the Council, the company has claimed that this is the best solution, given the difficult terrain, the earthquake threat and the rainfall (see section 3.3.1).[127] Low infrastructure and maintenance costs are the main advantage attributed to riverine disposal. It is reasonable to assume that this has been a decisive factor for Freeport, an assumption supported by the company's marketing of itself as "*the world's lowest-cost copper producer*".[128] The Council infers that the description is correct as long as neither the current nor the future environmental costs are part of the calculation. This means, though, that it is the local community and future generations who must carry such costs related to Freeport's operations.

In 1991, at the time of Freeport's contract renewal, it was internationally known what kind of environmental damage riverine disposal may lead to.[129] The OPIC review refers to Freeport's own documents, which predict that the emissions will cause increased sedimentation and change the shape of the whole river system.[130] According to statements made by CEO Bob Moffett, Freeport was aware that the tailings discharge also contained high copper levels, thus representing economic loss to the company.[131]

The Council regards riverine disposal as a conscious and planned choice on the part of Freeport. Moreover, the Council is of the opinion that Freeport knew riverine disposal could cause severe damage to the natural environment, but that the company and the Government attached little importance to environmental concerns.

The Council will also assess to which extent the company has implemented *adequate measures to rectify the damage*.

In the Council's opinion, it does not seem as if Freeport has taken appreciable measures to significantly reduce the damage to the environment. On the contrary, the company has substantially increased its production as compared with the conditions in the initial environmental approval, without adjusting the waste management accordingly (see sections 3.2 and 3.3.1). Given the scope of the devastation, the company does not inform how much the reclamation attempts in the deposition area (see section 3.3.1) actually will contribute to mitigate the damage.

Freeport calls attention to its comprehensive monitoring and control programme of the water quality in river systems and groundwater. The company also states that it performs other tests, for instance regarding metal content in sediments, plants and aquatic organisms. The test results are submitted to the Indonesian Ministry of the Environment on a quarterly basis. Allegedly, the results prove that contamination levels are within the official limits and that the mining does not cause severe irreversible environmental damage.[132] Still, the company chooses not to substantiate its claims, and the Council notes that the tests, as shown in section 3.3.1, indicate possible flaws in the company's arguments.[133]

In cooperation with its joint-venture partner, Rio Tinto, Freeport has conducted an extensive environmental risk assessment of its tailings management. The study was completed in 2002, and Freeport describes it as the result of comprehensive and thorough investigations, including more than 90 scientific surveys. According to Freeport, no new risks were identified in this process, and the diagnosed risks conformed to the impact anticipated in the environmental approval documents.[134] The company chooses not to inform which environmental effects were predicted in the Government concession or the risks that were identified through the investigations, nor does it provide any concrete information that may contribute to identify or evaluate the long-term environmental consequences associated with the mining operation, including the potential accumulation and release of heavy metals.

In the Council's view, the company is trying to create the impression that the environmental effects of its operation are negligible and do not leave any permanent impact. As there is no transparency in the company's environmental information, this is practically unverifiable. Since the company does not support its statements with data or scientific evidence, the assertions that emissions do not have any long-term adverse effects lack credibility.

The Council is of the opinion that Freeport has not focused on implementing measures to reduce the adverse effects of its mining operations, nor has the company wished to document its claims that the mining does not cause any severe environmental damage in the short or long run. This lack of environmental precaution and transparency increases the risk of the Fund's complicity in severe environmental damage.

Finally, the Council will evaluate whether *the company's unacceptable practice can be expected to continue in the future*.

The Grasberg mine is expected to operate until 2041, and Freeport has been given a licence to run the mine for another 30–40 years. The concession grants an annual extraction of 300,000 tons of ore. In its reports to the US Stock and Exchange Commission, Freeport informs that it plans to keep up the production volume in the years to come.[135] The company maintains that riverine disposal is the best waste management alternative, and it does not give any indication of intending to change this practice in the future or of implementing measures designed to significantly reduce the damage to the natural environment.

Hence, the Council deems it probable that the company's unacceptable practice will continue.

4.3 Conclusion

Based on the documents made accessible to the Council and Freeport's reply to the Council, the Council finds that Freeport's mining activities involve an unacceptable risk of complicity in severe and irreversible damage to the natural environment. In the Council's view, the company's practice of riverine disposal is in breach of international standards, and one may also question whether the company violates national environmental regulations. The company's assertions that its operations do not cause long-term irreversible environmental damage are hardly considered credible by the Council. The lack of openness and transparency in the company's environmental reporting reinforces this impression. Considering the plans presented by the company with regard to production increase and new prospecting there is reason to believe that the company's unacceptable practice will continue in the future.

5 Recommendation

After this assessment of the allegations against Freeport McMoRan Copper and Gold Inc., and in light of point 4.4 in the Ethical Guidelines, the Council recommends the company's exclusion from the *Government Pension Fund – Global*'s investment portfolio, owing to an unacceptable risk of complicity in present and future severe environmental damage.

Gro Nystuen	Andreas Føllesdal	Anne Lill Gade	Ola Mestad	Bjørn Østbø
(Chair)	(sign)	(sign)	(sign)	(sign)

Notes

1 In this paper also referred to as Freeport.
2 NOU 2003: 22, p 35.
3 Governmental White Paper on Ethical Guidelines, NOU 2003:22, p 167.
4 The Convention on Biological Diversity (5 June 1992); the World Heritage Convention (16 November 1972); the Convention on Long-Range, Transboundary Air Pollution (13 November 1979); the Vienna Convention for the Protection of the Ozone Layer (22 March 1985); the Stockholm Convention on Persistent Organic Pollutants (23 May 2001); the Basel Convention on Control of Transboundary Movements of Hazardous Wastes and their Disposal (22 March 1989); and others.
5 Vulnerability can be defined as an ecosystem's susceptibility to degradation or damage from adverse factors or influences. Resilience is an expression for the ability for an ecosystem to rebound from a disturbance.
6 Environmentally hazardous substances are characterised by the fact that they can cause damage even in small concentrations, due to their toxicity, their low degradability and/or accumulative potential in living organisms (bioaccumulation). The toxicity can be acute or cause long-term effects such as cancer, reproductive or genetic damage. Both heavy metals such as lead, cadmium and mercury, and organic substances such as PCB, DDT and dioxins are considered environmental toxins. It is not possible to determine safe levels for these substances in nature. Furthermore, environmental hazardous substances can be spread over long distances, even to other parts of the planet, where they may cause considerable damage to the environment and human health. See examples at Environmental Status in Norway, http://www.environment.no/templates/themepage____2153.aspx#B.
7 NOU 2003: 22, p 34.
8 NOU 2003:22, p 167.
9 According to Økokrim (the Norwegian National Authority for Investigation and Prosecution of Economic and Environmental Crime), environmental crime includes crime against nature, fauna and cultural heritage, as well as illegal pollution, see http://www.okokrim.no/menyen/hva _er_miljokrim.html.
10 NOU 2003:22, p 167.
11 NOU 2003:22, p 167.
12 The NGOs' websites are the following: http://www.eng.walhi.or.id/; http://www.jatam.org/english/index.html; http://www.mpi.org.au/; http://www.globalwitness.org/.
13 Bryce, Robert 1996: *Spinning Gold*, can be found at www.motherjones.com; Project Underground 1998: *Risky Business. The Grasberg Gold Mine. An Independent Annual Report on P.T. Freeport Indonesia*, see http://www.moles.org/ProjectUnderground/downloads/riskybusiness.pdf; Global Witness 2005: *Paying for Protection. The Freeport mine and Indonesian security forces*, available at http://www.globalwitness.org/
14 Global Witness 2005: *Paying for Protection*, p 12.
15 Global Witness 2005: *Paying for Protection*; Perlez, Jane and Bonner, Raymond: *Below a Mountain of Wealth, a River of Waste,* New York Times 27 December 2005, can be accessed at http://select.nytimes.com/gst/abstract.html?res=FB0C15F839540C748EDDAB0994DD404482.
16 Perlez, Jane and Bonner, Raymond: *Below a Mountain of Wealth, a River of Waste,* New York Times, 27 December 2005; Siboro, Tiarma: *Companies urged to stop paying soldiers*, Jakarta Post, 30 December 2005.
17 Abbreviation SEC.
18 Perlez, Jane and Bonner, Raymond: *New York Urges U.S. Inquiry in Mining Company's Indonesia Payment*, New York Times, 28 January 2006.
19 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, pp 6-7.
20 New Guinea is the world's second biggest island. One half of it, Papua, is Indonesian territory, whereas the other half belongs to Papua New Guinea.
21 International Crisis Group 2002: *Indonesia: Resources and Conflict in Papua.* ICG Asia report no 39, Chapter V, can be accessed at www.crisisweb.org.
22 The armed forces are also involved in large-scale economic activity, including security assignments for private companies, but also illegal activities such as gambling, blackmailing, prostitution and illegal logging and fishing. Estimates indicate that around 70% of the military's activities are still financed outside the Government budget even if a law from 2004 obliges the military to withdraw from all economic activity within 5 years. (Economist Intelligence Unit: *Country Profile Indonesia 2005*, p 10).

23 Indonesia ruled Papua, which until then had been a Dutch colony, under a UN mandate from 1962 to 1969. In 1969 Papua was annexed by Indonesia. The present Government has expressed support for a special form of self-rule in Papua. (Economist Intelligence Unit: *Country Profile Indonesia 2005*).

24 Economist Intelligence Unit: *Country Profile Indonesia 2005*

25 See footnote 24; World Bank Group Indonesia 2003: *Indonesia Environment Monitor 2003*, p 31, available at http://www-wds.worldbank.org/servlet/WDS_IBank_Servlet?pcont=details&eid=000012009_20030716161307.

26 Freeport-McMoRan Copper&Gold Inc. *Form 10-K Filings to the Stock and Exchange Commission (SEC) 2004*, p 8, see http://www.sec.gov/Archives/edgar/data/831259/000083125905000021/fcx200410-k.htm.

27 See footnote 26, p11; Freeport 2006: *Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund*, p 2. In its reply to the Council, Freeport states that the company after 2015 expects the production of ore to be reduced to 200,000 tons per day and the opencast mining to cease. Underground mining does not produce overburden.

28 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, p 2.

29 Freeport-McMoRan Copper&Gold Inc. Form 10-K Filings to the Stock and Exchange Commission (SEC) 2004, p 23.

30 See footnote 28.

31 See footnote 29, p 17.

32 Information on file with the Council. The source refers to Freeport's own documents: AMDAL 300K (1997), an environmental impact assessment, and the Environmental Risk Assessment (2002) commissioned by Freeport and Rio Tinto.

33 Information on file with the Council. The source refers to Freeport's own documents: AMDAL 300K (1997), fig. 5.6 a: "*Cumulative production from beginning of PTFI operations*".

34 Main sources: International Institute for Environment and Development (IIED) 2002: *Mining for the Future*. Appendix A *Large Volume Waste Working Paper*, Mining, Minerals and Sustainable Developmental Project, can be found at http://www.iied.org/mmsd/, US Environmental Protection Agency 1997: *Potential Environmental Impact of Hard Rock Mining*, see http://cfpub.epa.gov/npdes/indepermitting/mining.cfm; www.miljostatus.no, *Drainage from Mines*.

35 See footnote 28, p 8.

36 An estuary is a transition zone between the river mouth and the sea where freshwater from the river is mixed with more saline seawater. Low flow contributes to the deposition of finer sediments that often form a delta. Estuaries are valuable habitats for marine life, birds and other fauna.

37 IIED 2002: *Mining for the Future*. Appendix J *Grasberg Riverine Disposal case study*. Mining, Minerals and Sustainable Development Project.

38 The map on the left is from Freeport's SEC Filings 2004, p 4. The one on the right has been taken from Mining for the Future 2002: *Grasberg Riverine Disposal*, p J-4.

39 Suspended solids are particles floating ("in suspension") in the water.

40 Information on file with the Council. The reference here is to Freeport's own monitoring reports to Indonesian authorities for the second quarter of 2005.

41 Quoted in Perlez, Jane and Bonner, Raymond: *Below a Mountain of Wealth, a River of Waste,* New York Times 27 December 2005.

42 *Government Regulation 82/2001 Regarding Water Quality Management Water Pollution Control* establishes four different maximum limits for water pollution depending on the water's use. Class 1 is the most rigorous and is applicable to drinking water, whereas Class 4 is the least restrictive, destined for "*gardens and other uses.*" Maximum suspended solids content is set at 50 mg/l for drinking water and 400 mg/l in Class 4, see also footnote 41.

43 PT Freeport Indonesia 2005: *Riverine Tailings Transport*, p 4, see www.fcx.com.

44 IIED 2002: *Mining for the Future*. Appendix J *Grasberg Riverine Disposal Case Study*, p J-6. In the mid-1990s the aggradation of rock mass and sediment blocked the river, forcing it to seek a new course and spreading the discharges to an adjacent river system (the Minajerwi River). As a result and in order to contain the deposition area, Freeport initiated the construction of levees in 1997.

45 See footnote 44. Freeport, referred to in the New York Times 27 December 2005 (see footnote 41), declares that the levees designed to contain the tailings are expected to reach a height of more than 20 m in certain places in the lowland.

46 Information on file with the Council. Reference is made to Indonesian ministerial memorandums citing AMDAL 300K: "Estimates of materials balance suggest that a large portion of tailings (37 %) have flowed into the Arafura Sea and it is estimated that this portion may increase to 50 %."

47 Perlez, Jane and Bonner, Raymond: *Below a Mountain of Wealth, a River of Waste,* New York Times 27 December 2005, quoted from one of Freeport's former employees who worked with waste management until 2004.

48 See footnote 44, p J-9.

49 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, p 9.

50 See footnote 49.

51 Freeport and joint-venture partner RioTinto commissioned the American consultancy firm Parametrix to conduct a study on the environmental and health risks associated with tailings deposition. The report was concluded in 2002. The dispersion of emissions to the sea is described in Vol.1, Aquatic Ecological Risk Assessment (August 2002), on file with the Council.

52 See footnote 49.

53 EnviroSearch International 1994: *Environmental Review of PT Freeport Indonesia Copper and Precious Metals Mine Irian Jaya, Indonesia*, submitted to the Overseas Private Investment Corporation (OPIC), p 13.

54 IIED 2002: *Mining for the Future*, Appendix J: *Grasberg Riverine Disposal Case Study*, Table J2. The table is based on Freeport's own measurements.

55 In Norway copper is classified as an environmental toxin due to properties such as bioaccumulation and toxicity at low concentrations. The poisonous effect of copper on aquatic organisms is relatively well documented; see for example http://www.epa.gov/waterscience/criteria/copper/pdf/master.pdf and http://www.miljostatus.no/templates/pagewide____2828.aspx.

56 http://www.miljostatus.no/templates/themepage____2912.aspx,

57 Government Regulation 82/2001 Regarding Water Quality Management Water Pollution Control establishes a maximum limit of 0.02 mg/l copper in drinking water. Humans normally have a higher tolerance to copper than aquatic organisms. The drinking water standards also take into account that water is commonly transported through pipes which may release copper. Drinking water standards are thus no guarantee that aquatic organisms will not be affected. Limits established to prevent damage to water organisms are usually lower; see also footnote 667.

58 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, p 13. Freeport declares: *"Our monitoring of surface and groundwater shows dissolved copper levels well below the standard. Our monitoring of locally caught seafood and of plants grown on soils containing tailings show they are safe to consume. Extensive studies performed in our Environmental Risk Assessment show that copper in tailings poses negligible risk to aquatic organisms and terrestrial plants and animals. In addition, the same studies showed copper in our tailings poses no risk to human health."*

59 See footnote 58.

60 The Overseas Private Investment Corporation (OPIC) was established in 1971 as a self-sustaining U.S. government development agency whose mission is to mobilize and facilitate the participation of United States private capital and skills in the economic and social development of less developed countries and areas, and countries in transition from nonmarket to market economies. Among other things, the agency offers companies insurance against political risk, see http://www/opic.gov/.

61 EnviroSearch International 1994: Environmental Review of P.T.Freeport Indonesia Copper and Precious Metals Mine Irian Jaya, Indonesia; submitted to the Overseas Private Investment Corporation.

62 See footnote 61, p 9.

63 Information on file with the Council. These results are on a level with Indonesian drinking water standards, see footnote 57.

64 Refers to test point S260 just outside the deposition area. According to a report from the Indonesian Ministry of the Environment from November 1994, more than 25 per cent of the samples showed a copper concentration higher than 0.03 mg/l. Information on file with the Council.

65 Perlez, Jane and Bonner, Raymond: Below a Mountain of Wealth, a River of Waste, New York Times, 27 December 2005.

66 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, p 13.

67 Rather than to compare copper levels with drinking water standards, the Council considers it more relevant to look at water quality standards for freshwater which focus on various parameters with an impact on aquatic organisms. Australian water quality standards (ANZECC Water Quality Guidelines) use 0.001 and 0.0025 mg/l copper as tolerance limits for aquatic life, while American water quality standards (USEPA Aquatic Life Copper Criteria (Nov 2003)) establish a maximum of 0.0042 mg/l copper. According to the Norwegian Pollution Control Authority's (SFT) water quality criteria, freshwater with a copper content above 0.006 mg/l is classified as severely polluted. In Norway the goal is to reach a copper concentration of 0.01 mg/l in river systems polluted by acid rock drainage from mining. This goal is meant to ensure that biological life is preserved despite the run-off from mines. See http://deh.gov.au/water/quality/nwqms/volume1.html, http://www.epa.gov/waterscience/criteria/copper/pdf/master.pdf and http://www.miljostatus.no/templates/themepage____2912.aspx#A

68 The bioaccessibility of metals will vary according to the pH, the content of organic and particulate material, the water's hardness and other factors.

69 EnviroSearch International 1994: Environmental Review of P. T.Freeport Indonesia Copper and Precious Metals Mine Irian Jaya, Indonesia, pp 12–13; submitted to the Overseas Private Investment Corporation.

70 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, p 13.

71 OPIC letter to Freeport McMoRan 1995. OPIC discovered that Freeport had doubled its production volume without informing the agency and draws the following conclusion in its letter: "If OPIC had, prior to the issuance of the Contract, understood that the Project's ore and tailings production rates would be at such high levels, (and that such unreasonable or major environmental, health or safety hazards would result), the agency clearly would not have issued the subject policy." Available at http://www.foe.org/international/shareholder/OPICletter.htm

72 Gedicks, Al 2005: West Papua: The Freeport/Rio Tinto Campaign, in Moody, Roger 2005: The Risks We Run International Books; Perlez, Jane and Bonner, Raymond: Below a Mountain of Wealth, a River of Waste, New York Times, 27 December 2005.

73 See footnote 70, p 14, see also footnote 72.

74 Perlez, Jane and Bonner, Raymond: Below a Mountain of Wealth, a River of Waste, New York Times, 27 December 2005.

75 See footnote 74 with reference to the environmental risk assessment drawn up by Freeport and Rio Tinto. See also footnote 51.

76 See footnote 74.

77 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, p 8.

78 See footnote 77.

79 IIED 2002: Mining for the Future, Appendix J: Grasberg Riverine Disposal Case Study, p J-9.

80 Walhi/Friends of the Earth Indonesia 2003: *Undermining Indonesia, Adverse Social and Environmental Impacts of Rio Tinto's Mining Operations in Indonesia*, p 20, can be accessed at http://www.eng.walhi.or.id/kampanye/tambang/050228_undermining_rep/

81 Information on file with the Council.

82 See footnote 79.

83 See footnote 77, p 11

84 See footnote 77.

85 See footnote 77, pp 11–12.

86 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, p 12.

87 Freeport 2004: *Making the Commitment. Working towards Sustainable Development*, p 33; see footnote 86, p 22.

88 Information on file with the Council.

89 See footnote 88 with reference to Freeport's environmental risk assessment.

90 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, pp 9, 11, 12 and 16.

91 See footnote 90, p 8.

92 IIED 2002: Mining for the Future. Appendix J Grasberg Riverine Disposal case study, p J-11.

93 See for example Moody, Roger 2005: *Freeloading Freeport* in The Risks We Run. Mining, Communities and Political Insurance. International Books.
94 Abigail Abrash 2004: *Mining a Sacred Land*. Carnegie Council on Ethics and International Affairs, available at http://www.cceia.org/viewMedia.php/prmTemplateID/8/prmID/4459; see also footnote p 112.
95 Gedicks, Al 2005: *West Papua: The Freeport/Rio/Tinto Campaign,* p 112. In Moody, Roger 2005: The Risks We Run. Mining, Communities and Political Insurance. International Books.
96 See footnotes 94 and 95; Amnesty International USA: *Business and Human Rights – The Environment/ Freeport McMoRan in Papua*, available at http://www.amnestyusa.org/business/environment/indonesia.html
97 OPIC letter to Freeport McMoRan 1995, see http://www.moles.org/ProjectUnderground/motherlode/freeport/opicletter.html
98 See footnote 94.
99 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, pp 3–7
100 See footnote 99, pp 3–4.
101 See footnote 99, pp 3–4.
102 Information on file with the Council.
103 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, p 2; Freeport-McMoRan Copper&Gold Inc. Form 10-K Filings to the Stock and Exchange Commission (SEC) 2004, p 11, based on Freeport's records of rock output and ore production.
104 See p 11, based on information on file with the Council. The source refers to Freeport's own documents: AMDAL 300K (1997), and Freeport and Rio Tinto's Environmental Risk Assessment (2002).
105 Perlez, Jane and Bonner, Raymond: *Below a Mountain of Wealth, a River of Waste,* New York Times, 27 December 2005.
106 See footnote 105.
107 Bryce, Robert: *Printed in Stone*. The Austin Chronicle, 23 September 2005, available at http://www.austinchronicle.com/issues/dispatch/2005-09-23/pols_feature.html; IIED 2002: *Mining for the Future*. Appendix J *Grasberg Riverine Disposal case study*, p J-7; see also footnote 105.
108 See footnote 105.
109 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, p 17.
110 Freeport 2004: Making the Commitment. Working towards Sustainable Development, p 38.
111 The quotations are taken from Freeport's reply to the Council, see footnote 109, pp 17–18.
112 ARD is short for *Acid Rock Drainage*.
113 PT-FI is short for PT Freeport Indonesia, i.e. Freeport.
114 Tempo Interactive: *Freeport Not Licensed to Dispose of Tailing Waste.* Tempo Interactive, Jakarta, 6 January 2006. The newspaper quotes Rasio Ridho Sani, Assistant to the Minister for Poisonous and Dangerous Materials (B3) Waste Management Affairs: "*There has not yet been any licence issued by the state Ministry for the Environment for this*", see http://www.tempointeractive.com/.
115 Antara News: *Damage Caused by Freeport to Environment is Serious: Minister Says.* Antara News, 26 January 2006, available at http://www.antara.co.id/en/seenws/?id=8484.
116 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, p 10.
117 Perlez, Jane and Bonner, Raymond: Below a Mountain of Wealth, a River of Waste, New York Times, 27 December 2005; information on file with the Council.
118 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, p 24.
119 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, p 1.
120 http://www.europa.eu.int/comm/environment/waste/mining/index.htm.
121 IFC 2004: Environmental, Health and Safety Guidelines for Precious Minerals Mining. Draft available at www.ifc.org.

122 The Extractive Industries Review was launched by the World Bank Group to discuss its future role in the extractive industries with concerned stakeholders. The aim of this independent review was to produce a set of recommendations that will guide involvement of the World Bank Group in the oil, gas and mining sectors. Information and reports available at www.worldbank.org.

123 Mining, Minerals and Sustainable Development (MMSD) was an independent two-year process of consultation and research with the objective of understanding how to maximise the contribution of the mining and minerals sector to sustainable development at the global, national, regional and local levels. MMSD was a project of the *International Institute for Environment and Development* (IIED) commissioned by the *World Business Council for Sustainable Development* (WBCSD). For information and reports, see http://www.iied.org/mmsd/.

124 EIR 2004: Striking a Better Balance - The World Bank Group and Extractive Industries: The Final Report of the Extractive Industries Review, p 33; available at http://siteresources.worldbank.org/INTOGMC/Resources/finaleirmanagementresponse.pdf.

125 IIED 2002; Mining, Minerals and the Environment, chapter 10, p 250, in Breaking New Ground: Mining, Minerals, and Sustainable Development, Mining, Minerals and Sustainable Development Project; can be found at http://www.iied.org/mmsd/finalreport/index.html.

126 At the root of this decision lies the environmental devastation caused by riverine tailings disposal at the OK Tedi mine in Papua New Guinea, which BHP co-owned with the Papua New Guinean state until 2002. Because of the environmental damage BHP wanted to close the mine down earlier, but this was unacceptable to the authorities in Papua New Guinea, who took over the mine in 2002; see www.bhpbilliton.com.

127 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, pp 8 and 16. According to OPIC's review, other alternatives were presented in connection with the concession application, but were dismissed without sufficient and consistent analysis. See EnviroSearch International 1994: Environmental Review of P.T.Freeport Indonesia Copper and Precious Metals Mine Irian Jaya, Indonesia, submitted to the Overseas Private Investment Corporation, p 14.

128 See Freeport's home page: http://www.fcx.com/aboutus/co-overvw.htm

129 In the article Unearthing Controversy at the OK Tedi Mine from 2003 Polly Ghazi states: "In 1992, a group of indigenous landowners presented their grievances against Ok Tedi Mining to the International Water Tribunal in The Hague. The tribunal's judgments lack legal force. But its 1992 ruling, that the Papua New Guinea government should either prevent further damage or close the mine, brought Ok Tedi into the international spotlight." The article is published in World Resources Institute Features, July 2003, Vol.1, No.6, see http://newsroom.wri.org/wrifeatures_text.cfm?ContentID=1895&NewsletterID=39.

130 EnviroSearch International 1994: Environmental Review of P. T.Freeport Indonesia Copper and Precious Metals Mine Irian Jaya, Indonesia, submitted to the Overseas Private Investment Corporation, Appendix 016.2.

131 Project Underground 1998: Risky Business. The Grasberg Gold Mine. An independent Annual Report on P.T.Freeport Indonesia, p 15. In 1997, Mr Moffett claimed that the company's discharges equalled 200 tons of copper a day.

132 Freeport 2006: Response of FCX to the Draft Report by the Advisory Council on Ethics for the Norwegian Government Petroleum Fund, pp 12–13.

133 The company claims that its environmental analyses are accessible to the public. Nevertheless, they are available neither on the company's nor the Ministry's web sites. Freeport has informed the Council that one can gain access to these through the Ministry of the Environment's archives in Jakarta.

134 See footnote 132, p 24.

135 Freeport-McMoRan Copper&Gold Inc. Form 10-K Filings to the Stock and Exchange Commission (SEC) 2004, p 16.

Letter to the Ministry of Finance

Oslo, March 22, 2006

Regarding Aracruz Celulose S.A.

Reference is made to the Ministry of Finance's letter of 23 August 2005 in which the ministry forwards a request from five Brazilian organisations to exclude Aracruz Celulose S.A. from the investment universe of the then Government Petroleum Fund, now the Government Pension Fund – Global.

Aracruz, the world's largest producer of bleached eucalyptus pulp, recorded a turnover of USD 685.9 million in 2005. At the end of 2005 the Government Pension Fund – Global held shares worth NOK 34 682 million in the company, equivalent to an ownership share of 0.14 per cent.

Aracruz is alleged to have unlawfully acquired lands traditionally belonging to the Indian peoples in the area. These communities are demanding the return of the lands in question based on the constitutional rights of indigenous peoples in Brazil. Aracruz asserts that the properties were lawfully acquired from their legitimate owners, and that this is documented by land deeds.

The land conflict goes back to 1979. Since then a process has been under way involving the authorities in the shape of the Ministry of Justice along with Brazil's National Indian Foundation (FUNAI), representatives of Indian communities and Aracruz. Under an agreement with the Indian communities (dating from 1998, revised in 2002), Aracruz committed itself to contributing about NOK 1.4 million annually to fund development projects over a 20 year period, and has given up just over 2 500 hectares to the Indian Reservation.

However, the Indian communities claim they are entitled to a further 11 000 hectares which they assert that FUNAI, in a study from 1997 and most recently in a report of 20 February 2006, regard as Indian territory. Aracruz rejects this claim, pointing out that it has not previously been supported by the Minister of Justice. As far as the Council is aware, the issue is to be reviewed by FUNAI's legal affairs office and thereafter forwarded to the Minister of Justice for decision. According to Aracruz' website, the company would prefer the matter to be resolved by the courts.

As the Council sees it, this is primarily a conflict about land rights between Indians and Aracruz, although environmental issues and worker rights have been a matter of concern in this conflict as well. Indigenous peoples' rights to land is an important question. As regards the request from Brazilian organisations forwarded by the ministry, the Council bases its position on the fact that a process is in train with a view to resolving the conflict. The Council also attaches importance to the Brazilian authorities' engagement in the case and the fact that all stakeholders seem to be involved in the process The Council will await further developments before considering the need for a more thorough assessment of this case.

Yours sincerely,
Gro Nystuen
Chair of the Council on Ethics

To the Ministry of Finance

Oslo, April 18, 2006
(Published April 18, 2006))

Supplementary Recommendation on EADS Co.

Introduction

The exclusion of EADS from the investment universe of the Government Pension Fund – Global has been reviewed.

There is no longer a basis for exclusion of the company from investments related to involvement in the production of cluster munitions.

The recommendation to exclude the company is however upheld because the company is involved in production of key components to nuclear weapons.

Background

On 16 June 2005, the Advisory Council on Ethics for the Government Petroleum Fund submitted its recommendation on exclusion of companies that are involved in the production of cluster munitions.[1] The company EADS (European Aeronautic Defence and Space Company) was among the companies that were recommended for exclusion.

The basis for the exclusion of EADS was that the company in a letter to Norges Bank dated June 8, 2005, stated that the company owned the company TDA in a joint venture with the company Thales S.A. Moreover, EADS stated that TDA produced the mortar ammunition PR Cargo, which the Council considered to be cluster ammunition according to the Fund's ethical guidelines.

In a new letter to Norges Bank, dated 21 March, 2006, EADS stated that the company no longer is an owner of TDA and, thus, that there is no longer a basis for exclusion of the company from investments related to involvement in production of cluster munitions.

On 19 September 2005, the Council submitted its recommendation on exclusion of companies that develop and produce nuclear weapons.[2] EADS is mentioned in this recommendation because of its ownership in the company MBDA and its involvement in the development of the nuclear missile M51. Because EADS had already been excluded for its involvement in production of cluster munitions, the company was not again recommended for exclusion on the basis of its involvement in the production of nuclear weapons.

Further details on MBDA and M51

EADS owns 37,5 % of the company MBDA.[3] MBDA is, according to *Jane's Air Launched Weapons*[4], under contract to develop the ASMP-A missile for the French Air Force. ASMP-A is described as a "*nuclear warhead air-to surface missile*". ASMP-A will,

according to *Jane's*, be fitted with a nuclear warhead supplied by the French Government's CEA (*Commissariat á l'Energie Atomique*). The contract was signed in 1996 and final deliveries will be made in 2008.

MBDA displays components of ASMP-A on its internet homepage.[5] ASMP-A is not known to have applications other than to deliver nuclear warheads.

EADS is also involved in the development of the M51 missile.

Jane's Missiles and Rockets wrote on 2 February, 2005[6]: "*EADS SPACE Transportation has signed a contract with the French armament procurement agency (DGA) for production of the M51 submarine-launched ballistic missile (SLBM) The contract covers series production of the M51 weapon system for a period of 10 years. Worth more than EUR3 billion (US$4 billion), it includes a fixed tranche and several conditional options. EADS SPACE Transportation is prime contractor for the programme, while SNECMA, SNPE, DCN, Thales and Sagem are the main subcontractors…The M51 missile will enter service in 2010 on board the ballistic-missile submarine Le Terrible, followed by Le Vigilant, Le Triomphant and Le Téméraire after retrofit…The new missile weighs more than 50 tonnes compared with the 35 tonnes of the current M45. Maximum range will be more than 6,000 km, with altitudes of up to 1,000 km at the peak of its trajectory. It has an increased payload capacity and a higher accuracy than the M45. The M45 can carry up to six TN-75 warheads, each with an estimated yield of 100 kT.*"

This information pertains to the development of a new missile system (M51) for strategic nuclear weapons for the French navy. Exact data for the weapons are not publicly available, but it is compared to the existing M45, which has six warheads, each with a yield equivalent to 100 000 tons of TNT.

EADS has also described the development of M51 on its own homepages: "*EADS SPACE Transportation is prime contractor for the ballistic missile systems in France's nuclear deterrent force. The company is responsible for the development and production of the M45 and M51 submarine-launched missiles, as well as for their operating systems and maintenance. Since 1971, the company has overseen the development of five generations of strategic missiles, helping to ensure that France's nuclear deterrent force is effective and operational at a moment's notice.*"[7]

In its letter to Norges Bank dated 21 March 2006, EADS confirms its involvement in MBDA and in the development of the M51: *"On the other hand, our participation in MBDA and in the French M51 program is unquestionable. Unjustified association of EADS with cluster bomb business could impact EADS reputation in Norway."*

The Council has previously considered missiles that have no other application than to deliver nuclear warheads to be key components to nuclear weapons.[8] Thus, by contributing to the production of the ASMP-A and M51 missiles, the Council regards EADS as being involved in the production of key components to nuclear weapons.

Recommendation

The Council on Ethics for the Government Pension Fund – Global finds that the basis for excluding EADS from investments related to production of cluster munitions is no longer valid.

At the same time, it is clear that the company is involved in the production of nuclear weapons in a way that render recommendation of exclusion from the Fund. The recommendation to exclude EADS from the Government Pension Fund – Global is therefore upheld. The basis for the exclusion is that the company contributes to the production of key components to nuclear weapons.

Gro Nystuen	Andreas Føllesdal	Anne Lill Gade	Ola Mestad	Bjørn Østbø
(Chair)	(sign)	(sign)	(sign)	(sign)

Notes

1 See http://odin.dep.no/etikkradet/english/documents/099001-210003/dok-bn.html
2 See http://odin.dep.no/etikkradet/english/documents/099001-990075/dok-bn.html
3 Ownership structure described on MBDA's homepage: http://www.mbda.net/site/FO/scripts/siteFO_contenu.php?lang=EN&noeu_id=37
4 Database supplied by Jane's Information Group, see www.james.com
5 http://www.mbda.net/site/FO/scripts/siteFO_contenu.php?noeu_id=77&lang=ENU
6 Database supplied by Jane's Information Group, see www.james.com
7 Seehttp://www.eads.com/web/lang/en/1024/content/OF00000000400004/6/03/31000036.html
8 See http://odin.dep.no/etikkradet/english/documents/099001-990075/dok-bn.html

Letter to the Ministry of Finance

Oslo, 15 May 2006

Regarding investments connected to the Middle East

Background

On 6 January 2006 the Ministry of Finance received a letter from the Church of Norway Council on Ecumenical and International Relations concerning "*investments in the West Bank*". It urged the Government Pension Fund – Global to "*review its investments and possibly withdraw from companies that are active in the construction of the wall and Israeli settlements in the occupied West Bank. This also applies to infrastructure linked to the settlements, such as water and roads.*" The Council on Ecumenical and International Relations also requested a meeting with representatives from the Council on Ethics to discuss the issue in further detail.

The letter was submitted to the Council on Ethics for the Government Pension Fund – Global on 10 February 2006.

At a meeting held on 7 March 2006 the Council on Ethics discussed the Fund's possible contribution to violations of human rights or other ethical norms through investments in Israeli companies. The debate also covered investments in non-Israeli companies that have operations in or supply products to Israel, and whether these may constitute such contribution.

On 21 March 2006 the Council on Ethics' Chair and Secretariat had a meeting with representatives from the Council on Ecumenical and International Relations. After this the Council on Ethics has also engaged in further discussions on the issue.

This letter intends to give an account of the Council on Ethics' considerations regarding the aforementioned investments and the outcome of the meeting with representatives from the Council on Ecumenical and International Relations.

The Fund's investments in Israeli companies and institutions

On 10 February 2006 the Council on Ethics' Secretariat contacted Norges Bank to enquire about Israeli companies included in the portfolio and benchmark index of the Government Pension Fund – Global. Norges Bank replied to the inquiry on the same date, informing that the Fund's benchmark portfolio established by the Ministry of Finance does not include Israel, but that Israel is a country where investments can be made outside benchmark.

As of 10 February 2006 the Fund had investments in five Israeli companies / institutions, of which three were allocated to equities and two to bonds:

Equities

- **Bank Hapoalim BM** International bank for corporate and private clients.[1]
- **Emblaze Ltd** IT company (software), makes products such as digital video and mobile phone systems.[2]
- **Teva Pharmaceutical Industries Ltd** Pharmaceutical company, produces mainly generic drugs. 90 % of sales stem from markets in North America and Europe.[3]

Bonds

- **Israel Electric Corp** Energy company which is responsible for all electricity supply in Israel. The company is 99.8 % state-owned.[4]
- **Israel AID** Securities issued by the Israeli government, but guaranteed by the US government through US AID.

The Council on Ethics' assessment of the operations run by the Israeli companies and institutions included in the Fund

The Council on Ethics has no information to indicate that the companies selected for equity investments can be said in any way to contribute to Israeli authorities' possible violations of human rights or other ethical norms. Moreover, the Council on Ethics has no reason to believe that these companies contribute to the construction of the controversial wall which is being erected by the Israeli government or the maintenance of Israeli settlements in occupied territories. Such contribution hardly seems plausible in light of the companies' business areas. The Council on Ethics has therefore not found reason to proceed with any detailed assessment of these companies' possible complicity in violations.

Additionally, the Council on Ethics has analysed whether the investment in Israel Electric Corporation may constitute a contribution to violations provided that the company supplies electric power to illegal Israeli settlements. Even though the Council Ethics does not know exactly how the electricity supply to Israeli settlements in the West Bank is handled or what role Israel Electric Corporation plays, the Council does not consider the Fund's Ethical Guidelines to target such activities. In the Council's view, the supply of electric power to civilians can hardly be considered illegal or unethical. Besides, the maintenance of such infrastructure will be beneficial to all parties in the area.

The letter from the Council on Ecumenical and International Relations also refers to the exclusion of the company Kerr McGee Corp. from the Fund because of its offshore activities in Western Sahara5: *"The Council on Ecumenical and International Relations would like to point out that Norwegian authorities in a case related to Western Sahara have emphasized that investments in business activities in occupied areas are contrary to international law and Norwegian policy."*

The Council on Ethics is of the opinion that the comparison with the recommendation to exclude Kerr McGee Corp. should not be stretched too far. The background for Kerr McGee's exclusion was the company's contribution to the exploitation of natural resources in occupied territory. International law, including the UN Charter and the UN Convention on the Law of the Sea, says that activities which include the exploitation of natural resources in occupied, non-autonomous or other dependent areas shall be carried out in accordance with the wishes of the affected population. This is related to the fact that access to natural resources often is at the root of occupations and violent conflicts. Inter-

national law seeks to delegitimize financial gains acquired by the exploitation of natural resources through occupation. Even if it may be unclear whether the offshore exploration activity in Western Sahara constitutes a direct violation of international law, the Council on Ethics' assessment has been that the contribution to such activity must, at any rate, be regarded as a serious violation of basic ethical norms and therefore be covered by the Fund's Ethical Guidelines. However, the exclusion of Kerr McGee does not imply that the Fund's Ethical Guidelines apply to every kind of investment in occupied areas.

With regard to the Fund's investments in securities issued by Israel AID, the Council on Ethics has not made any assessment. It is beyond the mandate of the Council on Ethics to evaluate investments in government bonds.

The Council on Ethics' assessment of non-Israeli companies that do business in Israel

Concerning contribution to Israeli authorities' violations of human rights or other ethical norms, non-Israeli companies can also be assessed and thus fall within the scope of the Fund's Ethical Guidelines. This may be the case with companies that supply military equipment or civilian equipment with military applications to Israeli authorities.

The Council on Ethics is aware that a large number of companies provide Israel with military equipment. As a basis, the Council on Ethics accepts that the Israeli state has a legitimate right to keep military forces, and that the sale of military equipment to Israel will not, in itself, be targeted by the Fund's Ethical Guidelines, as long as this does not include weapons subject to the Fund's specific exclusion criteria for inhumane weapon types. An assessment of possible complicity in breaches of ethical norms must therefore be limited to companies that sell equipment while knowing it will be used exclusively for illegal or unethical acts.

In this context, the Council on Ethics has assessed the Fund's investment in the US company Caterpillar Inc.[6] The background for the Council's assessment is as follows:

Caterpillar Inc. supplies the Israeli Army with bulldozers and spare parts. In principle these are civilian machines, which in Israel are armoured and equipped for military use. Such armoured bulldozers have been used by the Israeli Army against Palestinian civilians, for instance to tear down Palestinian settlements and destroy Palestinian farmland. The Council on Ethics is also aware that lawsuits have been lodged against the company on the grounds of alleged complicity in human rights violations through the sale of military equipment to Israeli authorities.

The Council on Ethics deems it clear that Israeli authorities have used equipment supplied by Caterpillar to commit acts which probably can be considered as amounting to human rights violations. However, since the equipment Caterpillar delivers to Israeli authorities also is destined for legitimate use, it is problematic to hold the company accountable for all uses of its products. The Council on Ethics takes as a basis that, similarly to other military equipment, including different types of legal weapons, the applications may be both legitimate and legal, but the equipment may also be used for acts which must be considered unethical or even illegal. In the same way as for the components of inhumane weapons, which have several areas of use (see discussion of "*dual use*" in the recommendation on exclusion of companies that manufacture components for nuclear weapons), the main rule will be that such products do not fall within the scope of the Fund's Ethical Guidelines.[7] Consequently, there must be a strong element

of complicity by Caterpillar in any possible violations if the company is to be excluded in spite of this. The Council on Ethics assumes that it will be difficult to find facts which will provide grounds for exclusion of the company based on its supply of materials to the Israeli authorities.

Meeting with representatives of the Council on Ecumenical and International Relations

The Council on Ethics' Chair and Secretariat had a meeting on 21 March 2006 with the General Secretary, Olav Fykse Tveit, and two other representatives of the Council on Ecumenical and International Relations.

During the meeting a briefing was given on the Fund's Ethical Guidelines in general and the Council on Ethics' assessment of investments in Israeli companies included in the Fund. On its own initiative, the Council on Ecumenical and International Relations raised the issue of Caterpillar, and the Council on Ethics' view of the company's possible contribution to violations was presented orally. Subsequently, the comparison with the exclusion of Kerr McGee was discussed, and the Council on Ethics pointed out that this case has little relevance to the conflict between Israel and the Palestinians.

Conclusion

The Council on Ethics has not found grounds for recommending the exclusion of companies because of their activities in Israel or in areas under Israeli occupation. This applies to both the Israeli companies in the Fund and the foreign companies with operations in the area. A meeting has been held with representatives from the Council on Ecumenical and International Relations during which this assessment was presented. However, the possibility is not ruled out that information may be revealed in the future leading to closer examination and possible recommendations.

Yours faithfully,
Aslak Skancke p.p.
Senior Adviser
Secretariat to the Council on Ethics for the Government Pension Fund – Global

Notes

1 See http://www.bankhapoalim.com/
2 See http://www.emblaze.com/contact.asp
3 See http://www.tevapharm.com/
4 See http://investor.i-ecnet.co.il/
5 See recommendation on the exclusion of Kerr McGee Corp., 12 April 2005: http://odin.dep.no/etikkradet/norsk/dokumenter/099001-990062/dok-bn.html
6 See http://www.cat.com/
7 See the Council on Ethics' recommendation on the exclusion of companies that develop and produce nuclear weapons, 19 Sep 2005: http://odin.dep.no/etikkradet/norsk/dokumenter/099001-990072/dok-bn.html

To the Ministry of Finance

Oslo, May 24, 2006
(Published September 1, 2006)

Recommendation on suspension of exclusion of KerrMcGee Corporation

1 Background

The Council on Ethics for the Government Petroleum Fund, now the Government Pension Fund – Global, ("the Council"), submitted a recommendation to the Ministry of Finance on May 12, 2005, on the exclusion of KerrMcGee from the Fund's investment universe.

The company was, through its subsidiary KerrMcGee de Maroc Ltd, involved in exploration and survey activities for mapping of oil and gas resources on the continental shelf off Western Sahara. For reasons detailed in the recommendation on exclusion, the Council considered these activities to be in breach of the Fund's ethical guidelines' point 4.4, "other particularly serious violations of fundamental ethical norms".[1]

The Ministry of Finance decided to follow the Council's recommendation and instructed Norges Bank on April 29, 2005 to exclude the KerrMcGee from the Fund's investment universe. The Fund's holdings in the company were sold and the Ministry of Finance published its decision on June 6, 2005.[2]

On May 3, 2006, the Council wrote to KerrMcGee to enquire whether the company's activities on the continental shelf off Western Sahara were terminated.

In a letter dated May 10, 2006, KerrMcGee confirmed that the company has ceased its activities in the Boujdour field and that the licence to conduct explorations had expired in April 2006.

2 The Council's assessment

Point 4.6 of the Fund's ethical guidelines state the following:
"The Council shall review on a regular basis whether the reasons for exclusion still apply and may against the background of new information recommend that the Ministry of Finance revoke a decision to exclude a company."

Based on the new information that has been received by the Council, the activities that formed the basis for the Council's recommendation to exclude the company have now ended. The Council therefore finds that the basis for exclusion of KerrMcGee from the investment universe of the Government Pension Fund – Global no longer exist.

3 The Council's recommendation

The Council on Ethics recommends that the Ministry of Finance annuls its decision to exclude the company KerrMcGee from the investment universe of the Government Pension Fund – Global. This recommendation is founded on point 4.6 of the Fund's ethical guidelines, which warrants recommendation to revoke decision of exclusion when the reason for the exclusion no longer applies.

This recommendation is submitted on May 24, 2006, by the Council on Ethics for the Government Pension fund – Global.

Gro Nystuen	Andreas Føllesdal	Anne Lill Gade	Ola Mestad	Bjørn Østbø
(Chair)	(sign)	(sign)	(sign)	(sign)

Notes

1 The recommendation to exclude KerrMcGee is dated April 12, 2005: http://odin.dep.no/etikkradet/english/documents/099001-230017/dok-bn.html

2 Press release from the Ministry of Finance, June 6, 2005: http://odin.dep.no/fin/english/topics/pension_fund/p10002777/pressreleases/006071-070639/dok-bn.html

To the Ministry of Finance

Oslo, September 6, 2006
(Published December 6, 2006)

Recommendation on exclusion of Poongsan Corporation

1 Background

Point 4.4 of the Ethical Guidelines for the Government Pension Fund – Global, states the following: *"The Council shall issue recommendations on negative screening of one or several companies on the basis of production of weapons that through their normal use may violate fundamental humanitarian principles."* In the Government White Paper on Ethical Guidelines (NOU 22: 2003), and through the subsequent discussion of the Guidelines in the Storting (Parliament), cluster munitions were considered as falling within this category of weapons.

Based on the above, the Council, on June 16, 2005, issued its recommendation on exclusion from the Fund of companies that produce cluster munitions.[1] This recommendation provided for a closer description of cluster munitions, as well as a description of which weapons' components fall within the Fund's guidelines. The recommendation also stated: "*It is emphasized that this recommendation does not contain an exhaustive list of possible producers of cluster weapons, and that new recommendations concerning the exclusion of companies on this basis may be given later.*"

2 Further details on cluster munitions produced by Poongsan Corporation

The South Korean company Poongsan Corp. produces various types of munitions for military use, including 155 mm artillery shells. On its website, the company describes two of these products.[2] The shell designated DP-ICM TP is described as containing 88 "*bomblets*", i.e. small, explosive submunitions that characterize cluster munitions. Furthermore, the shell designated DP-ICM K305 is described as follows: "*This is fired from 155 howitzer and used for blast, fragmentation, mining effects.*" In this context, it appears that the company, by using the term "*mining effects*", specifically promotes that this type of munitions have a high failure rate which leads to a large number of undetonated explosives on the ground, with similar effects as antipersonnel landmines.

At the Council's request, Norges Bank has written to the company in order to inquire whether the company produces cluster munitions. The company was asked to answer the following question:

"In connection with the implementation of these Guidelines we have been asked by the Advisory Council on Ethics for the Government Petroleum Fund to enquire whether it is correct that your company, or subsidiaries of your company, are producing, assembling or planning to produce or

assemble: key components to air delivered or surface delivered cluster dispensers such as aerial bomb dispensers, rockets or other containers, and/or sub-munitions for such dispensers, such as ICM (Improved Conventional Munitions) or DPICM (Dual Purpose Improved Conventional Munitions)/CEM (Combined Effects Munitions)."

The company did not respond to the letter from Norges Bank.

The Council on Ethics assumes that the information provided on the company's website is up to date and thus concludes that the company produces cluster munitions.

3 Recommendation

The Council recommends exclusion of the company Poongsan Corporation from the investment universe of the Government Pension Fund – Global. This recommendation is based on Point 4.4 of the Fund's Ethical Guidelines which prescribes exclusion of companies *"on the basis of production of weapons that through their normal use may violate fundamental humanitarian principles"*.

This recommendation is submitted on September 6, 2006, by the Council on Ethics for the Norwegian Government Pension Fund – Global.

Gro Nystuen	Andreas Føllesdal	Anne Lill Gade	Ola Mestad	Bjørn Østbø
(Chair)	(sign)	(sign)	(sign)	(sign)

Notes

1 Recommendation given 16. June, 2005: http://odin.dep.no/etikkradet/english/documents/099001-210003/dok-bn.html

2 Company homepage: http://www.poongsan.co.kr/english/

Ethical Guidelines for the Government Pension Fund – Global

This translation is for information purposes only. Legal authenticity remains with the original Norwegian version.

Ethical Guidelines Norwegian Government Pension Fund – Global

Issued 22 December 2005 pursuant to regulation on the Management of the Government pension Fund – Global, former regulation on the Management of the Government Petroleum Fund issued 19 November 2004.

1 Basis

The ethical guidelines for the Government Pension Fund – Global are based on two premises:

- The Government Pension Fund – Global is an instrument for ensuring that a reasonable portion of the country's petroleum wealth benefits future generations. The financial wealth must be managed so as to generate a sound return in the long term, which is contingent on sustainable development in the economic, environmental and social sense. The financial interests of the Fund shall be consolidated by using the Fund's ownership interests to promote such sustainable development.
- The Government Pension Fund – Global should not make investments which constitute an unacceptable risk that the Fund may contribute to unethical acts or omissions, such as violations of fundamental humanitarian principles, serious violations of human rights, gross corruption or severe environmental damages.

2 Mechanisms

The ethical basis for the Government Pension Fund – Global shall be promoted through the following three measures:

- Exercise of ownership rights in order to promote long-term financial returns based on the UN Global Compact and the OECD Guidelines for Corporate Governance and for Multinational Enterprises.
- Negative screening of companies from the investment universe that either themselves, or through entities they control, produce weapons that through normal use may violate fundamental humanitarian principles.
- Exclusion of companies from the investment universe where there is considered to be an unacceptable risk of contributing to:
  - Serious or systematic human rights violations, such as murder, torture, deprivation of liberty, forced labour, the worst forms of child labour and other child exploitation
  - Grave breaches of individual rights in situations of war or conflict
  - Severe environmental damages
  - Gross corruption
  - Other particularly serious violations of fundamental ethical norms.

3 The exercise of ownership rights

3.1 The overall objective of Norges Bank's exercise of ownership rights for the Government Pension Fund – Global is to safeguard the Fund's financial interests. The exercise of ownership rights shall be based on a long-term horizon for the Fund's investments and broad investment diversification in the markets that are included in the investment universe. The exercise of ownership rights shall primarily be based on the UN's Global Compact and the OECD Guidelines for Corporate Governance and for Multinational Enterprises. Norges Bank's internal guidelines for the exercise of ownership rights shall stipulate how these principles are integrated in the ownership strategy.

3.2 Norges Bank shall report on its exercise of ownership rights in connection with its ordinary annual reporting. An account shall be provided of how the Bank has acted as owner representative – including a description of the work to promote special interests relating to the long-term horizon and diversification of investments in accordance with Sections 3.1.

3.3 Norges Bank may delegate the exercise of ownership rights to external managers in accordance with these guidelines.

4 Negative screening and exclusion

4.1 The Ministry of Finance shall, based on recommendations of the Council on Ethics for the *Government Pension Fund – Global*, make decisions on negative screening and exclusion of companies from the investment universe.

The recommendations and decisions shall be made public. The Ministry may, in certain cases, postpone the time of public disclosure if this is deemed necessary in order to ensure a financially sound implementation of the exclusion of the company concerned.

4.2 The Council on Ethics for the *Government Pension Fund – Global* shall consist of five members. The Council shall have its own secretariat. The Council shall submit an annual report on its activities to the Ministry of Finance.

4.3 Upon request of the Ministry of Finance, the Council issues recommendations on whether an investment may constitute a violation of Norway's obligations under international law.

4.4 The Council shall issue recommendations on negative screening of one or several companies on the basis of production of weapons that through normal use may violate fundamental humanitarian principles. The Council shall issue recommendations on the exclusion of one or several companies from the investment universe because of acts or omissions that constitute an unacceptable risk that the Fund contributes to:

- Serious or systematic human rights violations, such as murder, torture, deprivation of liberty, forced labour, the worst forms of child labour and other forms of child exploitation
- Grave breaches of individual rights in situations of war or conflict
- Severe environmental damages
- Gross corruption
- Other particularly serious violations of fundamental ethical norms

The Council shall raise issues under this provision on its own initiative or at the request of the Ministry of Finance.

4.5 The Council shall gather all necessary information at its own discretion and shall ensure that the matter is documented as fully as possible before making a recommendation regarding negative screening or exclusion from the investment universe. The Council may request Norges Bank to provide information as to how specific companies are dealt with in the exercise of ownership rights. Enquiries to such companies shall be channelled through Norges Bank. If the Council is considering recommending exclusion of a company, the company in question shall receive the draft recommendation and the reasons for it, for comment.

4.6 The Council shall review on a regular basis whether the reasons for exclusion still apply and may against the background of new information recommend that the Ministry of Finance reverse a decision to exclude a company.

4.7 Norges Bank shall receive immediate notification of the decisions made by the Ministry of Finance in connection with the Council's recommendations. The Ministry of Finance may request that Norges Bank inform the companies concerned of the decisions taken by the Ministry and the reasons for the decision.

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Trykksak

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Design Tori Falch
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