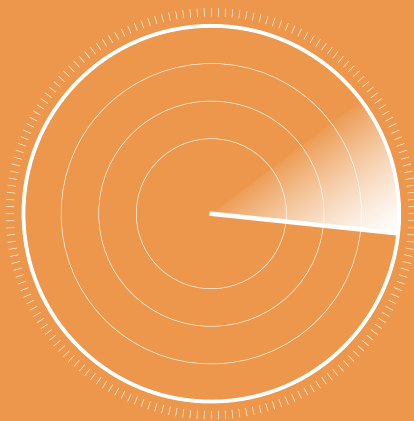


# Council on Ethics

for the Norwegian Government Pension Fund Global



## Annual Report 2017



**The Council on Ethics gives recommendations  
to Norges Bank on observation and exclusion of  
companies from the Norwegian Government  
Pension Fund Global**

**[etikkradet.no](http://etikkradet.no)**

# Contents



The Chair's report	5
Members of the Council and the Secretariat	6
The work of the Council on Ethics	7
The Council's work under the human rights criterion	15
The Council's work under the coal and climate criteria	18
Exclusion of nuclear weapons producers	21
Shipbreaking	25
List of excluded companies	28
List of companies under observation	29
<b>Recommendations on exclusion and observation</b>	
Published recommendations and observation letters	31
• Bharat Heavy Electricals Ltd.	33
• PetroChina Co Ltd.	33
• Leonardo SpA	35
• Eni SpA	36
• Saipem SpA	38
• Hansae Yes24 Holdings Co. Ltd. og Hansae Co. Ltd.	39
• AECOM	41
• Atal SA	41
• BAE Systems Plc.	42
• Fluor Corp., Huntington Ingalls Industries Inc., Honeywell International Inc.	42
• Evergreen Marine Corp. (Taiwan) Ltd.	43
• Korea Line Corp.	43
• Pan Ocean Co. Ltd.	44
• Precious Shipping PCL	44
• Thoresen Thai Agencies PCL	45
• Observation letter on Petróleo Brasileiro SA	46
<b>Guidelines for observation and exclusion from the Government Pension Fund Global</b>	<b>51</b>



# Annual report

---



# The Chair's report

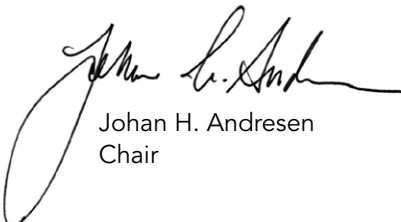
The Council on Ethics' mandate makes it unique. The fact that the Council's recommendations are made public, combined with the size of The Norwegian Government Pension Fund Global (GPF), means that exclusions do not go unnoticed. The fund's emphasis on responsible investment management is something many people admire, but it would not be possible without an independent ethical advisor.

2017 was another busy year for the Council on Ethics. Working with large individual companies and engaging them in dialogue has become more demanding. We have devoted considerable resources to examining potential violations of human rights. Last year, for the first time, we assessed the position of shipping companies which dispose of vessels to be broken up for scrap on the beaches of Bangladesh and Pakistan. In addition, we have continued to examine the extent of child labour in India's seed production sector, working conditions at textiles factories in Southeast Asia, and the situation for migrant workers in the Gulf States. This latter is a risk that was previously under-reported, but which has come particularly to light in connection with the construction of the infrastructure required for the soccer World Cup in Qatar. The Council on Ethics will continue to work not only on these issues, but also on matters relating to the rights of indigenous peoples.

The climate criterion was included in the GPF's ethical guidelines in 2016. Over the course of last year, we established a practice for assessing whether emissions are unacceptable. It has been necessary to adopt a thorough and holistic approach to this, both because it will form the basis for future assessments, and because other investors may come to follow our line. The Council on Ethics has issued some recommendations under this criterion, and more will follow. The shared operationalisation of the coal criterion, under which Norges Bank has had primary responsibility for identifying companies, continues to work well.

While the Council's task is solely to assess the ethical risk, Norges Bank has a broader mandate and can attach importance to other factors and employ different tactics. Under the corruption criterion, for example, the bank decided in 2017 to place two companies under observation that the Council on Ethics had recommended be excluded and to exercise active ownership with respect to two companies that the Council had recommended be placed under observation. The Council is responsible for performing such observations, while Norges Bank is responsible for exercising active ownership. Ethical risks associated with corruption are difficult to assess and hard – though not impossible – to influence. Both observation and the exercise of active ownership can make an impact here. The Council's collaboration with Norges Bank is good and will continue to evolve, not least as a result of this division of responsibilities.

The world is becoming more open and accessible – both for the fund as an investor and for the Council as an assessor, analyst and advisor. Many organisations work hard to uncover problematic issues associated with businesses all over the world. For example, it is no longer hard to find information about where shipping companies have their vessels broken up. Now that information has become readily available, perhaps companies will also pay more attention to the value of a good reputation. At the same time, the fund is investing in a growing number of companies in countries where both the ethical risk and lack of transparency are substantial. Technological changes also create a risk of new types of norm violations. The Council on Ethics' challenge will be to keep sight of established risks while remaining alert to the emergence of new ones.



Johan H. Andresen  
Chair



# Members of the Council and the Secretariat

## The Council on Ethics



### Johan H. Andresen (Chair of the Council on Ethics)

Andresen holds an MBA from Rotterdam School of Management, Erasmus University. He is now the owner and chairman of Ferd, having been the CEO for 14 years. His previous positions include that of Product Manager for International Paper Co. in the US and partner at the Tiedemanns Group. He is a member of various boards, including SEB - Skandinaviske Enskilda Banken, NMI - Nordic Microfinance Initiative and Junior Achievement Europe.



### Hans Christian Bugge (Vice Chair of the Council on Ethics)

Bugge holds a doctorate in law from the University of Oslo and is currently Professor Emeritus at the Department of Public and International Law at the University of Oslo, focusing on national and international environmental law issues. He has previously held various civil service positions at the Ministry of Environment and Ministry of Finance, and been Director of the Norwegian Pollution Control Authority, Secretary General of Save the Children Norway and State Secretary in the Ministry of Development Cooperation.



### Cecilie Hellestveit

Hellestveit is a lawyer by background, with a doctorate in humanitarian law from the University in Oslo. She also holds a degree in area- and conflict studies, with a particular emphasis on the Middle East. Hellestveit has worked at various research institutions, including PRIO, SMR, NUPI, IKOS and ILPI. She has been a non-resident fellow at the Atlantic Council in Washington DC, and is currently employed by the Norwegian Defense Establishment. Hellestveit has previously held an appointment with the Immigration Appeals Board (UNE) and been a member of medical and health research ethics committees under South-Eastern Norway Regional Health Authority. She has served at the Norwegian Refugee Council's board of directors, and has been a columnist on foreign affairs in the weekly Morgenbladet and the financial newspaper Dagens Næringsliv.



### Trude Myklebust

Myklebust is a lawyer from the University of Oslo and holds a MSc (res) from the School of Geography and Environment at the University of Oxford. She is currently a PhD candidate at the University of Oslo's Department of Private Law. Myklebust spent many years at the Ministry of Finance, where she worked on ethical guidelines for and responsible management of Norway's Government Pension Fund, among other matters. Myklebust has previously served as a deputy judge, and as a senior advisor for the Director of the Supreme Court of Norway. She has also authored a textbook on financial market law.



### Brit Kristin Sæbø Rugland

Rugland holds a Master of Management degree from BI Norwegian Business School. She is the CEO of Rugland Investering AS, Stavanger Investering AS and Rugland Finans AS. Rugland was a member of Norges Bank's Executive Board from 2004 until 2013. In addition, she has served on the boards of Storebrand ASA (1995–2002) and Stavanger Aftenblad (2002–2010), and chaired the boards of Gassco AS (2001–2011) and Rogaland Theatre (2006–2016). Rugland currently sits on the boards of Talent Norge AS, Norfund and Kommunalbanken AS and is Figgjo AS' board chair.

## The Secretariat

The Council has a Secretariat that investigates and prepares cases for the Council. The Secretariat has the following employees:

- Eli Lund, Executive Head of Secretariat (Economist)
- Magnus Bain (Cand. jur.)
- Lone Fedders Dybdal (MPhil.)
- Kjell Kristian Dørum (Cand. polit.)
- Erik Forberg (Cand. scient)
- Pia Rudolfsson Goyer (Cand. jur)
- Hilde Jervan (Cand. agric)
- Aslak Skancke (Graduate Engineer)



# The work of the Council on Ethics

The Council on Ethics for the Government Pension Fund Global (GPF) is an independent body that makes recommendations to Norges Bank with regard to either excluding companies from the GPF or placing them under observation. The Council has five members and a secretariat with a staff of eight. The Council assesses a company's operations on the basis of guidelines determined by the Norwegian Ministry of Finance. The guidelines contain both product-based exclusion criteria, such as the production of tobacco, coal, or certain types of weapons, and conduct-based exclusion criteria, such as gross corruption, human rights violations, environmental damage and unacceptably high greenhouse gas emissions. The threshold for exclusion is intentionally high, and companies may be excluded only if they represent an unacceptable future risk to the fund's ethical standards.

All the Council's recommendations are published on its website as soon as Norges Bank has announced its decision.

## Activities in 2017

The Council on Ethics continuously monitors whether companies in which the GPF is invested could operate in ways that infringe the fund's guidelines for observation and exclusion. As a result, the Council works on many different cases and issues in parallel.

A consulting firm provides the Council with a quarterly report on any companies it has identified whose operations may infringe the guidelines' product criteria. The report also includes relevant new information on companies that are already excluded from investment by the fund. In addition, the Council follows up information provided by other sources and investigates all relevant companies on an ongoing basis.

With regard to the guidelines' behavioural criteria, companies are identified as a result of portfolio monitoring, external reporting and systematic reviews of areas associated with a high ethical risk. Every day, a consulting firm goes through a large number of news sources in several languages in search of relevant reports on companies in the GPF's portfolio. The Council receives bi-monthly reports from the consultants, and looks into those companies in which the risk of future norm violations seems high. When selecting cases to examine

in more detail, the Council gives weight to the violation's scope and seriousness, its consequences, the company's responsibility for or contribution to the matter concerned, the measures it has implemented to prevent or remedy the harm caused, and the risk of similar incidents occurring in the future. External reports are dealt with in the same way. In 2017, the Council had meetings with numerous organisations and individuals who wished it to investigate specific companies. The Council is currently in the process of assessing some of these companies in more detail.

Reviews of areas associated with a high ethical risk generally follow a long-term plan. Once the Council on Ethics has selected an area for examination, it follows through over a period of several years. For example, the Council has followed up textiles producers in some Southeast Asian countries since 2015.

The Council on Ethics obtains information from research environments as well as regional, national and international organisations, and often commissions third-party consultants to investigate indications of infringements of its guidelines. Furthermore, the companies in the GPF's portfolio are themselves important sources of information, with the Council frequently engaging in lengthy dialogues with company officials during the assessment process.



**Table 1. Activities undertaken by the Council on Ethics**

Year	2015	2016	2017
No. of limited companies in the GPFG at year-end (approx.)	9050	9000	9100
Total no. of companies excluded at the recommendation of the Council on Ethics at year-end	64	66 <sup>1</sup>	64 <sup>2</sup>
No. of companies placed under observation at the recommendation of the Council on Ethics	1	2	6
No. of recommendations made	8	9	11
No. of companies excluded during the year	4	5	1
No. of companies placed under observation during the year	1	1	4
No. of companies readmitted during the year	0	1	1
No. of companies the Council has contacted	42	86	62
No. of companies the Council has held meetings with	11	22	12
No. of new cases the Council has assessed	69	64	32
Total no. of companies under assessment during the year	184	162	149
Total no. of company assessments concluded during the year	73	53	75
No. of Council meetings	11	12	10
Secretariat (no. of staff)	8	8	8
Budget (NOK million)	14.8	15.9	18.1

The table presents a summary of the scope of the company assessments performed by the Council on Ethics in 2017 compared with 2016 and 2015. Those companies which Norges Bank has decided to exclude under the coal criteria without this being based on a recommendation by the Council on Ethics are not included in the table.

1. With effect from 2016, unlisted subsidiaries are not counted in the number of excluded companies. Three unlisted companies, which were excluded on their own account, are therefore not included in the number of excluded companies at the turn of the year.
2. Two companies have been delisted from the stock exchange and no trading in related debt instruments has been carried out in the market. They have therefore also been omitted from the list of excluded companies.

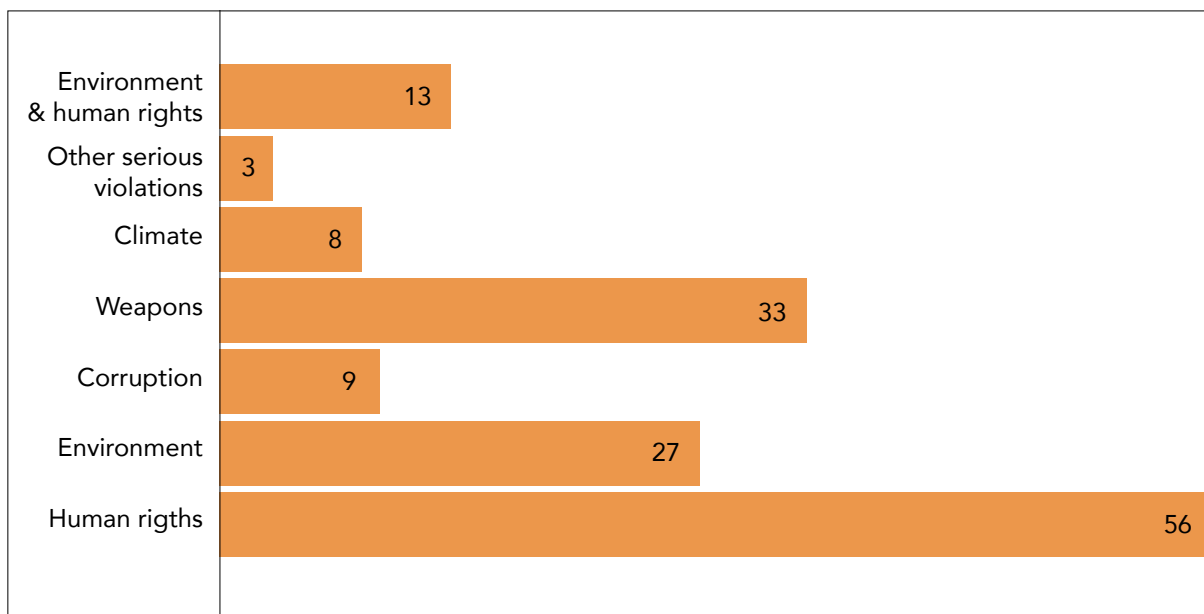
In 2017, the Council on Ethics issued 10 recommendations to exclude a total of 11 companies, and one recommendation to place a company under observation. On the basis of the Council's recommendations from 2016 and 2017, Norges Bank announced that one company had been excluded, one was readmitted and four had been placed under observation. The exercise of shareholder influence (active ownership) was the chosen strategy with respect to a further two companies. Following the close of 2017, Norges Bank has announced its decision to exclude a further nine companies and place one under observation. As at 1 March 2018, therefore, 73 companies have been excluded from investment by the GPFG, and seven placed under observation, on the basis of recommendations by the Council on Ethics. In addition, Norges Bank has, on its own initiative, excluded

69 companies and placed a further 13 under observation with reference to the coal criterion. The companies on which the Council has published recommendations since the previous annual report are described in more detail on page 31.

In 2017, the Council on Ethics assessed 149 companies. Of this number, 32 were new companies in 2017, while 75 ongoing assessments were completed during the year. The reduction in the number of new cases compared with 2016 is due to the fact that the Council initiated fewer new reviews of areas involving a high ethical risk. With regard to corruption, in particular, the Council has focused to a greater extent than before on individual companies that have been identified through general portfolio monitoring.



**Fig. 1. Cases under assessment, by criterion**



The figure shows which exclusion criteria the 149 companies examined by the Council on Ethics in 2017 have been assessed against.

The violation of human rights was the behavioural criterion against which the majority of companies were assessed in 2017. In recent years, the Council has devoted considerable resources to matters concerning labour rights. However, the number of companies being examined does not mean that the Council gives priority to human rights cases rather than, for example, climate-related cases. The Council applies very different approaches to the various criteria. While climate-related cases are often assessed on the basis of publicly available information, cases involving the violation of labour rights often require the Council to perform its own investigations. As a result, a larger number of companies are put under preliminary investigation in human rights cases, while the number of companies that are actually excluded is not as high.

Many companies have operations that may be covered by both the environmental criterion and the human rights criterion. Take, for example, the shipping companies that the Council on Ethics recommended in 2017 be excluded because they have sold ships to be broken up for scrap on the beaches of Bangladesh and Pakistan.

Both extremely poor working conditions and severe pollution have been reported in connection with this practice. The Council considers that the norm violations, both with respect to the environment and labour rights, are so serious that they each independently constitute sufficient grounds for the companies to be excluded.

In 2017, the Council on Ethics commissioned an external report on the production of nuclear weapons and the possible delimitation of the nuclear weapons criterion. Although the Council maintains its previous practice in such cases, it has – in connection with this report – considered more weapons cases than in recent years. Under the product criteria, all cases that are identified through portfolio monitoring are examined, because the guidelines state that all companies which produce certain, specified products must be excluded. Since the criteria have been the same for several years, and few new companies with such operations have come into the fund, work on the product criteria requires, in practice, less follow-up of individual companies than work relating to the behavioural criteria. For example, the Council was

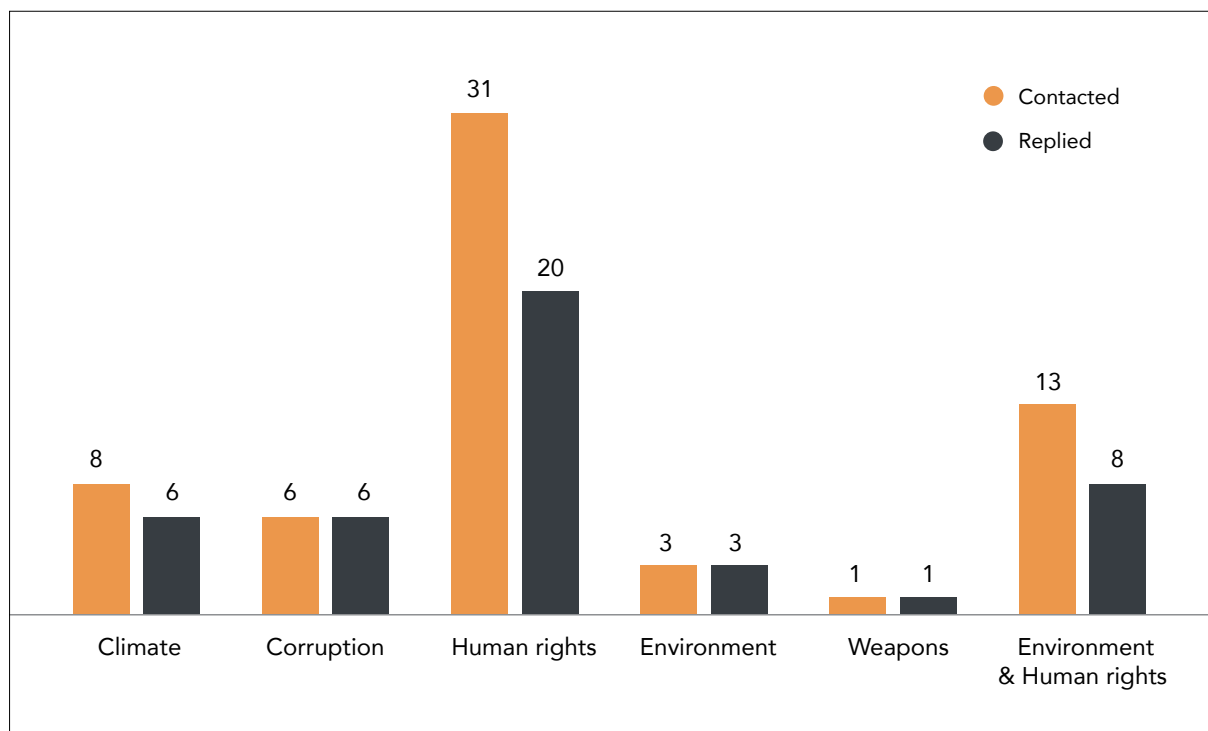
in contact with only one weapons-producing company in 2017. The Council's work with respect to the nuclear weapons criterion in 2017 is described on page 21.

Norges Bank may exclude companies under the coal criterion without any recommendation from the Council on Ethics. A division of labour has been agreed between Norges Bank and the Council, under which the bank identifies companies which fall within the scope of the criterion and will follow them up in future. The Council will assess those companies to which it may be alerted.

### Contact with companies in 2017

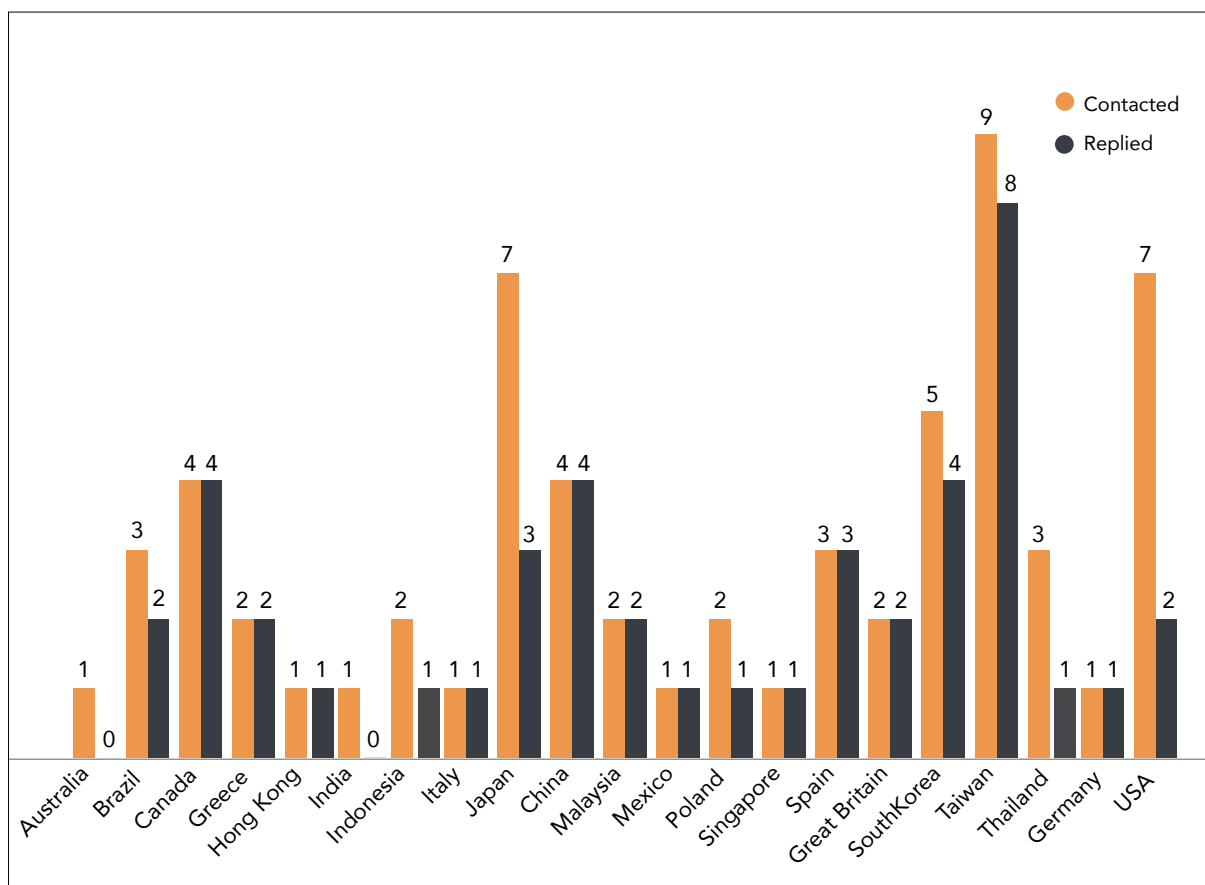
In 2017, the Council on Ethics contacted 62 companies and held meetings with 12 of them. The Council contacts companies which, after a preliminary examination, it has decided to assess in more detail. The Council first writes a letter to each company asking for documentation that could provide a better foundation for assessing its operations, e.g. working conditions or the recruitment of migrant labourers. Each company being assessed under behavioural criteria are also given the opportunity to comment on a draft report, before the Council sends its final recommendation to Norges Bank.

Fig. 2. Companies contacted with regard to each criterion



The figure shows how many companies the Council on Ethics has been in contact with in 2017, which criteria these companies are being assessed against, and how many of the companies have replied to the Council's questions.

Fig. 3. The countries in which the companies contacted by the Council are listed.

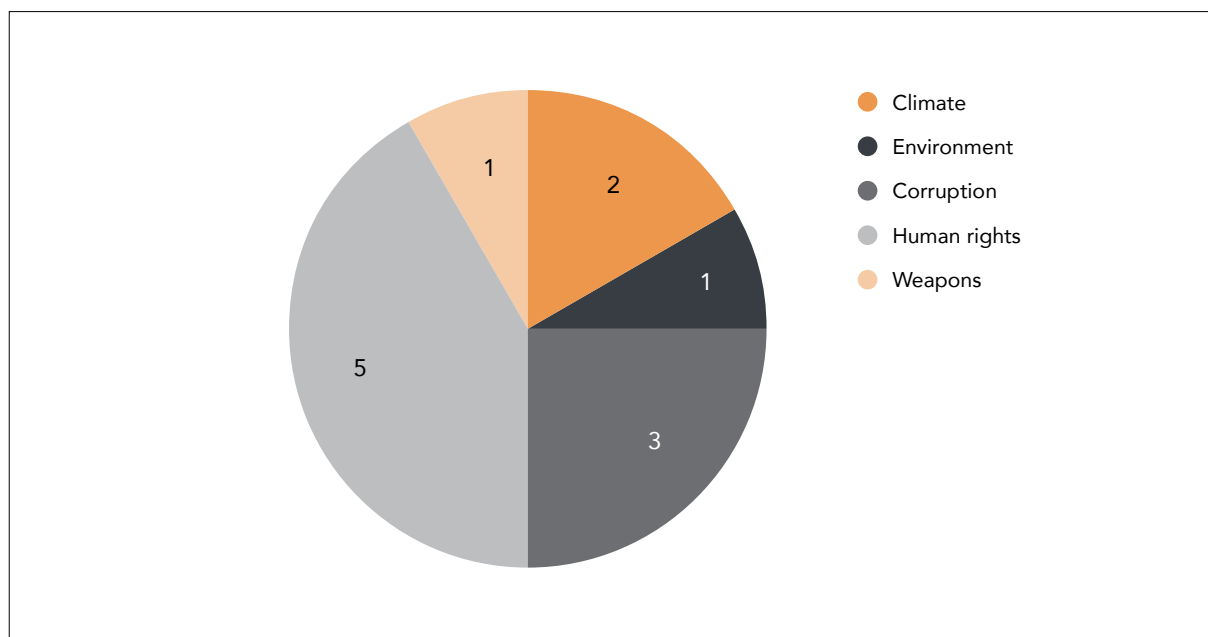


The figure shows where the companies with which the Council on Ethics has been in contact are listed, and whether the companies have replied to the Council's questions. Although the companies are widely spread geographically, the majority are located in Asia.

So far, 2/3 of the companies contacted by the Council on Ethics in 2017 have replied. This is slightly fewer than last year. The vast majority of companies avail themselves of the opportunity to comment on the Council's draft recommendation to exclude or place them under observation, although fewer reply to its initial letter of enquiry. The Council attaches importance to information provided by the companies, and considers it a risk factor if they do not provide tangible, verifiable information about their operations.

The Council on Ethics held fewer meetings with companies in 2017 than in 2016. This is because fewer companies were assessed under the corruption criterion. Since the assessment of a company's compliance systems is often a key element in corruption-related cases, the Council often holds face-to-face meetings with the companies concerned. In other cases, it is generally less necessary to meet company representatives, because the facts are more readily available. The purpose of meetings is to obtain information that enables the Council to determine whether there are grounds for a company's exclusion.

**Fig. 4. No. of companies the Council has met with in relation to each criterion**



The figure shows a breakdown of the meetings with companies in 2017 by criterion. Included in the overview are physical meetings as well as video and telephone conferences.

### Reassessment of excluded companies

Company exclusions are not time-limited. Companies may be readmitted to the GPF as soon as the grounds on which they were excluded no longer apply. Every year, the Council on Ethics performs a superficial assessment of all excluded companies to check whether they are still engaged in the activity which led to their exclusion, or whether their operations have materially changed. A more thorough examination is made of some companies, if they request it or there are indications of material operational changes. If a company has implemented measures that have led to sufficient changes in the factors upon which their exclusion was based, the Council issues a recommendation to revoke its exclusion. Any such improvements must be observable in practice, not just in the company's strategies and plans.

The Council on Ethics' recommendations to exclude are based on information about events that have occurred and the company's response thereto.

The recommendations published on the Council's website therefore represent a snapshot of the situation as it was when the company was excluded. Due to resource constraints, the Council does not normally issue new recommendations if a company continues to warrant exclusion from the GPF, even though the situation has changed over time. In some cases, however, such a long time has passed that the Council wishes to issue a new recommendation irrespective of whether the conclusion is to revoke or to uphold the exclusion.

### Observation

A company may be placed under observation if there are doubts about whether the conditions for exclusion have been met, about future developments, or in other circumstances where it is deemed appropriate. The Council on Ethics can itself recommend observation, but Norges Bank may also decide to place a company under observation where the Council has initially recommended its exclusion.

The Council on Ethics is responsible for following up companies that have been placed under observation on the basis of recommendations it has issued. Norges Bank is responsible for following up companies that it has placed under observation with reference to the coal criterion.

The Council on Ethics currently has seven companies under observation: three with respect to corruption, two with respect to human rights, one with respect to the environment, and one with respect to both human rights and the environment. The Council may, at any point during the observation period, recommend that a company be excluded or removed from the observation list.

During the observation period, the Council on Ethics provides Norges Bank with an annual assessment of the company. The Council obtains information from open sources and, in some cases, also from studies carried out by consultants. Sometimes, this information is sufficient to draw a conclusion, while at other times the Council may need to discuss it at a meeting with the company. In every case, a draft of the report to be sent to Norges Bank is also sent to the individual company for their comments. The observation process therefore depends on a good collaboration between the Council and the companies under observation.

### Ongoing and new assessments

With respect to the climate criterion, the Council is concentrating its focus on sectors whose overall emission levels are high. In addition to some types of oil extraction, the Council will focus its efforts in 2018 on companies that produce cement, steel or coal-fired electricity. The Council has already issued several recommendations under the climate criterion. However, as at 1 March 2018, Norges Bank had not published its final decision on these cases. See page 18 for further details of the Council's activities with respect to the climate criterion.

With respect to the environmental criterion, the Council has, since 2010, been working systematically in accordance with a long-term plan to examine all the companies in specific sectors or

areas where there is a particular risk that companies are causing serious environmental damage. In 2017, the Council carried out a new assessment in order to direct its efforts towards areas where the risk is greatest. Several of the focus areas from 2010 remain in effect, such as the destruction of tropical forests, threats to conservation areas, pollution from mining activities and fisheries that are particularly harmful to the environment. While efforts with respect to deforestation have so far concentrated on Asia and Africa, the Council will, in 2018, also assess companies that participate in deforestation in Latin America. Commercial meat and soya production are the most important reasons for forest loss in the region. The Council will initially assess companies that own land themselves, and that are therefore directly responsible for deforestation and the loss of biodiversity.

In 2017, the Council on Ethics embarked upon a review of companies that sell ships to be broken up for scrap in Bangladesh and Pakistan. The process, called *beaching*, involves ships being run aground at high tide, from where they are broken up manually. So far, four companies have been excluded and one company placed under observation on the grounds that their activities represent an unacceptable risk of contributing to both human rights violations and serious environmental damage. This work continues in 2018. See page 25 for further details of the Council's work with respect to beaching.

Since 2015, the Council has assessed a number of companies that produce textiles in some Southeast Asian countries. In 2017, the Council recommended that two such companies be excluded from the GPF. However, Norges Bank decided to place them under observation instead. The Council considers that a company's board and senior management must demonstrate that they take responsibility for working conditions at all levels in its operations, and establish management systems, incentives and control regimes that can secure acceptable working conditions. The Council will focus on this in its dialogue with the textiles companies that have been placed under observation. The Council will continue to examine working conditions in the textiles industry in 2018.

Under the human rights criterion, work continues with respect to conditions akin to forced labour for migrant workers and child labour in the production of hybrid seed varieties. See page 15 for further details.

Previous exclusions make it easier for the Council to pick up on similar new cases. The Council continues to monitor areas where the rules of occupation under international law may be applied, and companies that engage in the extraction of natural resources in disputed territories.

With reference to the corruption criterion, Norges Bank decided in 2017 to place two companies under observation whose exclusion the Council on Ethics had recommended at the close of 2016. Norges Bank considers that the steps taken by the companies to combat corruption constitute sufficient grounds to warrant a period of observation. When monitoring developments at these companies, the Council will attach importance to whether

they implement measures in accordance with international best practice for anti-corruption systems. In brief, this requires the companies to have the necessary structures, systems and routines in place to enable them to prevent, uncover and deal effectively with corruption. With reference to the corruption criterion, Norges Bank also decided in 2017 to exercise active ownership in the follow-up of two companies which the Council had recommended be placed under observation. Norges Bank is responsible for following up these companies.

Over the past couple of years, the authorities in several countries have uncovered and prosecuted cases of widespread corruption. This has led to many companies being picked up through the ordinary portfolio monitoring process. These cases will lay claim to a great deal of the Council's resources, in addition to cases remaining from its studies of the defence and petroleum industries.



## The Council's work under the human rights criterion

Section 3 of the GPFG's guidelines states that "Companies may be put under observation or be excluded if there is an unacceptable risk that the company contributes to or is responsible for serious or systematic human rights violations."



The Council on Ethics bases its assessment of what constitutes a violation of the human rights criterion on internationally recognised conventions and authoritative interpretations thereof. The Council examined many different issues relative to this criterion in 2017. The main focal points under this criterion were investigations into labour rights violations in the textiles industry in Southeast Asia, conditions akin to forced labor for migrant workers in the Gulf States and child labour in the seed production sector in India, as well as the break-up of ships for scrap in Bangladesh and Pakistan, which was assessed in relation to both the human rights and environmental criteria.

### **The textiles and garment industry**

In 2017, the Council on Ethics continued its examination of working conditions at companies which themselves produce yarn, fabric or garments. The Council has previously concluded that a small number of human rights violations can be sufficient to exclude a company if those violations are extremely serious, while violations do not individually need to be that serious if they occur systematically. In the textiles-related cases it has assessed, the Council considers whether a company is at risk of being responsible for systematic human rights violations.

For human rights violations to be systematic, they must be substantial in scope. In other words, they must be numerous, must infringe different types of rights or must occur in many different parts of the company. For the Council, "systematic" implies that such violations are not isolated incidents, but form a pattern of behaviour. In cases where violations of labour rights occur in a company's own operations, the company has direct responsibility for its employees and for preventing their labour rights from being infringed. The Council's position is that, with respect to norm violations perpetrated within a company's own operations, the threshold for what can be accepted must be lower than when a company contributes to norm violations perpetrated by others. In its assessment of the risk of human rights violations, the Council attaches importance to how a company has previously responded when norm violations have been uncovered, and what it has done to prevent such violations from occurring once again.

Since it started work in 2015, 17 companies have been assessed. A total of 25 factories have been investigated in Cambodia, Vietnam, Bangladesh and Myanmar, and further investigations are currently underway. For some companies, several factories have been investigated, or the same factory has been investigated on several different occasions.

The examination of working conditions at the factories is performed by consultants, partly through interviews with workers off site, at locations where they feel safe. Factory inspections have also been carried out. The investigations have shown that working conditions at the factories are generally poor, and that many operate in contravention of national legislation. Forced overtime, unlawful wage deductions, discrimination and harassment are common. In some factories, there are indications of working conditions that are harmful to health, due to result of excessive noise, heat, chemicals and high concentrations of dust. Managers at several factories have implemented measures to prevent unionisation. Child labour is unusual, but in some factories youngsters under the age of 18 work with no attention paid to their need for particular protection.

On the basis of the investigations carried out so far, draft recommendations to exclude have been sent to 12 companies. Several of the companies have subsequently contacted the Council and initiated measures to improve working conditions. Nevertheless, the question is whether such measures will have a lasting impact. Most textiles companies are inspected by customers or their representatives many times each year, and most customers demand that the companies respect human rights. When norm violations are uncovered, the companies draw up a plan for corrective action. However, the Council's investigations have revealed many labour rights violations in companies that are regularly inspected by customers. One explanation may be that the customers focus on the production line that manufactures for them, while the overall responsibility for working conditions at the company is addressed to only a lesser extent.

Assessing the threshold for what constitutes serious and systematic human rights violations as well as evaluating future risk, represents a major challenge. The Council has previously recommended the exclusion of two companies, which Norges Bank elected to place under observation. Work with respect to seven of the companies has concluded because the working conditions were not of such a nature as to warrant exclusion or because the companies have made significant improvements and changes in their management practices, which have helped to reduce the future risk. The Council's investigations show that there are major differences in working conditions at the textiles factories and in how the companies operate their businesses. If the board and management so wish, it is possible to be a responsible employer and provide acceptable working conditions at their factories.

The Council on Ethics will continue its work with textiles and garment manufacturers in 2018.

### **The construction industry and service sector in the Gulf States**

In 2017, the Council on Ethics has carried out a number of investigations into workers' situation in companies in the construction industry and service sector in Qatar and the UAE. The workers are almost all migrants from Nepal, Bangladesh, India and Pakistan. The Council found that it is common practice for workers to pay to get work in the Gulf States, and that many have taken out loans to cover the cost. During the recruitment process, workers are, moreover, often misled about working conditions and rates of pay. As a result, many become extremely dependent on their employer, so that the relationship borders to forced labour. Workers normally have little knowledge of their rights. Since the project's commencement in the autumn of 2016, nine companies have been investigated. The Council will continue this work in 2018.

### **Workers from North Korea**

In 2017, the Council on Ethics recommended the exclusion of a property developer because it knowingly employed a subcontractor that used North Korean labourers at one of its construction sites. Although the workers were not directly employed by the company in which the GPFG

had invested, the Council considers that the main contractor has a responsibility for all the workers at its construction sites. The Council attached importance to the fact that several UN reports point out that North Korean workers, who are hired out through North Korean staffing agencies, are subjected to forced labour. The workers are sent abroad by the regime without knowing the conditions they will be working under. They cannot choose to cease working, since their passports and mobile phones are confiscated. They live under constant surveillance and must remain either at the place of work or domicile. They work under the threat of reprisals against their families back home should they complain or abscond. This practice will probably be severely curtailed after the UN Security Council's recent decision to extend sanctions against North Korea, including a ban on the issuing of work permits to North Korean workers by member states.

### **Child labour in the seed industry**

In 2017, the Council on Ethics also carried out field studies to investigate the scope of child labour at several companies engaged in the Indian seed industry. The companies have been followed up in 2017. Following the Council's enquiries, two companies have made it clear that they will strengthen their efforts to reduce the use of child labour in their seed production. The Council on Ethics has decided not to recommend the exclusion of these companies at this juncture, but will instead monitor their performance over a period of time. Further follow-up of companies, as well as additional field studies relating to one company, will be carried out in 2018.

### **Individual cases**

The Council on Ethics often uses sector studies to identify and investigate companies deemed to have a high risk of violating ethical norms. Through news reports and other ad-hoc reporting, the Council also receives information about individual companies which may warrant further investigation. Individual cases that the Council has worked on in 2017 have related largely to the rights of indigenous peoples.



## The Council's work under the coal and climate criteria

In 2017, the Council on Ethics has issued several recommendations under the climate criterion, and will continue working with respect to the most emissions-intensive types of industry, such as the production of oil, steel and cement.

The climate criterion was introduced in 2016 and applies to “acts or omissions that on an aggregate company level lead to unacceptable greenhouse gas emissions”. The criterion’s wording is general and does not rest on any known norms or standards. It has therefore been necessary to identify a number of overarching factors which may be significant in the assessment of whether a company’s emissions are unacceptable.

The scope and availability of data and information varies substantially, and there may be systematic variations between countries, regions and business sectors. Not all companies report their emissions, and not all report their output of products in ways that can be compared. The extent to which companies publish details of other factors which could affect our assessment of their greenhouse gas emissions also varies.

In principle, the Council considers that to warrant exclusion under the climate criterion, a company must have a large overall emission volume, its emission level per unit produced must be higher than its competitors, and it must have no credible plans detailing how its emissions are to be reduced to an acceptable level within a reasonable period of time.

### **Relevant regulations and agreements**

The UN's Framework Convention on Climate Change, the Kyoto Protocol and the Paris Agreement are intended to cover the states which endorse them and give signatory states full control over how emission reductions are to be implemented. Practically every country in the world has signed the Paris Agreement. The Paris Agreement does not itself set emission levels for the business community as a whole or for individual companies. Nor does it set specific targets for emission reductions in the individual countries. However, it has been agreed that the overall objective is to keep global warming well below two degrees Celsius. There is also agreement on how large the emission reductions need to be to reach that goal. So far, the sum of all the national emission reduction targets is insufficient to reach this overall objective, but it is expected that the individual countries will gradually set national emission reduction targets that coincide with the global objective, and will choose appropriate measures to achieve it.

Different countries will adopt different approaches to reach their targets, based on a mixture of domestic political assessments and priorities, and country-specific opportunities. Nevertheless, it is the Council's opinion that no company with substantial emissions can decide simply not to set reduction targets for its own greenhouse gas emissions. The Council considers that companies

with substantial greenhouse gas emissions have an autonomous responsibility to contribute to the reduction in overall emission levels, and will attach importance to the extent to which the companies' own specific plans and targets coincide with the global emission-reduction goals.

### **Emission allowances and other measures**

A small number of countries have introduced various types of cap and trade systems. The EU's is the largest of these. Some other countries have introduced various types of carbon tax. At the moment, the EU's cap and trade system is based on a large proportion of cost-free allowances. There is also a large surplus of tradable emission allowances in the market, so prices are currently low and do not trigger much in the way of emission-reducing measures. However, because the EU has recently resolved to tighten up the regulations, this picture will change somewhat over time. Nevertheless, around half of the emissions generated within the EU are still not regulated by the cap and trade system. The majority of countries which have signed the Paris Agreement either plan to introduce cap and trade systems or wish to regulate national emissions in other ways.

When emission costs increase, certain types of production could be relocated to countries where the costs are lower, while others, such as power generation facilities, do not compete in the global market and could find it easier to pass the additional costs on their customers.

At present, the Council on Ethics does not place particular emphasis on whether companies produce emissions in countries with established cap and trade systems.

### **What can be compared?**

In the majority of cases assessed by the Council on Ethics, a company's behaviour must be compared with a norm of some sort. The Council's mandate under the climate criterion is to identify companies that produce unacceptable levels of greenhouse gas emissions. However, there are no established norms for what constitutes unacceptable emission levels. Instead, the Council will have to compare one company's emissions with another, similar



company's emissions, and assess whether the difference in emissions per unit produced warrants being characterised as unacceptable.

A further challenge is that such emission figures do not normally exist. Nevertheless, it is often possible to make an indirect comparison. If, for example, different types of raw materials or production technologies are used by the companies being compared, and these raw materials and technologies have known emission outputs, it may often be possible to estimate the differences in emission levels. This is something that requires substantial resources on the Council's part.

### **Parent companies and subsidiaries**

The grounds for exclusion are "acts or omissions that on an aggregate company level lead to unacceptable greenhouse gas emissions". For the Council on Ethics, the aggregate company level encompasses the company's entire production of the same class of goods. (This differs from the coal criterion, which states explicitly that it applies both to companies and to "entities they control".) As a result, no weight can be attached to activities in a company's parent or subsidiaries. This can be illustrated clearly if we look at a hypothetical example from the power generation sector:

The GPFG owns shares in Company A, which produces electricity. 95 per cent of Company A's output is either hydropower or wind power, while 5 per cent comes from old, inefficient power plants which burn brown coal. On an aggregate level, this results in a volume of emissions that is too small to qualify for exclusion. Then imagine that the coal-fired power division is transferred into another company, Company B, which Company A controls and in which the GPFG also owns shares. Company B produces no other kind of electricity. Company B therefore derives 100 per cent of its power output from outdated brown-coal power plants, and may be excluded from the GPFG on the grounds of the emissions they produce. In this case, it seems unreasonable to exclude Company A for the emissions of its subsidiary, since it would not have qualified for exclusion if the emissions had all been in the same company. Correspondingly, if the opposite were to happen and the hydropower and wind power operations were transferred to the

subsidiary, Company B, and only coal-fired electricity were retained in the parent company, Company A, the Council would be unable to attach importance to the emissions from Company B when the parent company, Company A, was being assessed.

With respect to the other behavioural criteria, the Council holds the general view that where one company (subsidiary) in which the fund invests is controlled by another company (parent) in which the fund also invests, the parent company is also responsible for the actions of the subsidiary. If a subsidiary is excluded because it has violated our guidelines, eg by causing serious environmental damage, the parent company must also be excluded.

### **Lobbying**

In most countries, the arrangement of measures intended to reduce national emission levels will be the outcome of complex assessments, in which their impact on businesses, employment, infrastructure, etc, may be given importance. In connection with such decision-making processes, it is usual for various company and commercial interests to present proposals and assessments of the measures' impact on their own business activities. In principle, such lobbying activities must be considered legitimate and can hardly be accorded any weight in our assessments. However, it is quite a different matter if companies attempt to mislead decision makers through statements they know to be false. The fact that information about such attempts to actively influence policy is not as readily available everywhere represents a challenge. In most countries, such processes take place largely behind closed doors.

### **The coal criterion**

The coal criterion was also introduced in 2016 and applies to "mining companies and power producers which themselves or through entities they control derive 30 per cent or more of their income from thermal coal or base 30 per cent or more of their operations on thermal coal". Implementation of this criterion is divided between the Council on Ethics and Norges Bank, with the main responsibility falling to Norges Bank.



## Exclusion of nuclear weapons producers

One of the tasks which falls to the Council on Ethics is to recommend the exclusion of companies that produce nuclear weapons. The GPFG's ethical guidelines on this issue, which have remained unchanged since 2004, state that:

“The Fund shall not be invested in companies which themselves or through entities they control: a) produce weapons that violate fundamental humanitarian principles through their normal use”.

In the revised national budget for 2004 and in subsequent reports to the Norwegian parliament (Storting) about the GPF's investment management, the Ministry of Finance has made it clear what types of weapons are meant, i.e. all classes of weapons that Norway is prohibited from using or possessing. In practice, the weapons criterion has resulted in the exclusion of companies producing antipersonnel landmines, cluster munitions and nuclear weapons.

It is worth noting that the Ministry of Finance has, in subsequent reports – most recently in Report No. 26 to the Storting (2016–2017), made it clear that the criterion encompasses the *production* and *development* of both the *weapons* themselves and the *key components of this type of weapon*.

A total of 16 companies are at present excluded from investment by the GPF because of their involvement in nuclear weapons production. In the spring of 2016, the Council on Ethics recommended the exclusion of four companies which produce key components of nuclear weapons, and the continued exclusion of one company on the basis of nuclear weapons production, but on other grounds than originally stipulated. Norges Bank agreed to implement the Council's recommendations in January 2018.

#### **Delimitation of the criterion, assessment of previous practice**

The production of nuclear weapons is extremely complex and they form part of weapons systems comprising a large number of components. This complexity creates challenging delimitation issues for the Council's application of the criterion. The preparatory work of the guidelines provides limited information, and no new guidelines on the matter have been issued since 2004.

On this basis, the Council on Ethics decided in the winter of 2017 to engage an external consultant to prepare a report covering:

- A description of nuclear weapons production as it is carried out today and expected future developments.

- An assessment of the Council's practice since 2005, with respect to consistency and compliance with the guidelines and preparatory works.
- A description and assessment of what may be deemed to constitute a nuclear weapon's *key components*.
- An assessment of what, in this context, falls naturally within the terms *production* and *development*.
- An assessment of other investors/funds' practice in this area.
- Proposals for the formulation of an exclusion criterion with respect to companies' products and business activities.

#### **Key findings and recommendations**

The report discusses in depth the term *key components*, including various approaches to limiting the definition of components with several purposes, so-called *dual-use* components. The terms *production* and *development* are also discussed.

On the basis of its review, the report proposes the following definition of the types of components that may constitute grounds for the exclusion of companies:

*«A single-purpose key component of a nuclear weapon is one that is specially designed, developed, produced, or adopted for use in a nuclear weapon system and that is essential for the intended use of a weapon.»*

This definition clarifies the fact that relevant components cannot have several uses (they must be *single-purpose*) and that the individual component's relative significance for other components in the weapon system must be such that it is essential for the weapon to function.

All the Council's recommendations to exclude nuclear weapons producers fall within the scope of this definition.



Furthermore, the report argues that so-called delivery platforms, which have no other purpose than the delivery of nuclear weapons, should be considered key components. The same may apply to components of such delivery platforms. In practice, this applies primarily to submarines and their component parts, but could also, for that matter, apply to vehicles and aircraft (and their component parts).

A review of other fund and investors' exclusions shows differing delimitation practices. Only a very few of those who exclude nuclear weapons producers have formulated an unambiguous definition of their exclusion criteria or exclude companies due to their production of delivery platforms. The number of investors who publish which companies they exclude, even if they have a policy of excluding nuclear weapons producers, is limited.

### **The Council on Ethics' conclusion**

Despite the development and production of nuclear weapons being strictly regulated and covered by an extensive framework of rules that are meant, among other things, to prevent their proliferation, there are surprisingly few clear definitions of what a nuclear weapon actually is (and, not least, what key components are). The Council on Ethics therefore has a fairly large amount of leeway to exercise its own best judgement. The report provides a useful overview of various approaches to the delimitation of the criterion.

The proposed definition of the term *key components* seems sensible as a guide to the Council's further work on the criterion. But not even such a definition resolves all the problems relating to delimitation.

The report's examination of the Council's recommendations shows no companies with operations considered to fall outside a reasonable delimitation of the criterion.

Nor does the report point to any areas or companies which should obviously have been considered for exclusion, given the delimitation of the criterion practised by the Council.

Another question is whether the Council should expand the limits of what should be covered by the criterion. In particular, the report points out that the exclusion of those producing strategic submarines and some of their components would be in line with the proposed definition. Several countries have extensive programmes for the construction of new strategic submarines, and a large number of companies will be involved in supplying components for them.

The Council on Ethics takes the position that even if the proposed definition is applied, other considerations could indicate that the criterion's limits should not be expanded in this direction:

In the guidelines' preparatory works, exclusion on the grounds of nuclear weapons was not envisaged because it was assumed that all such activity would be carried out by state-owned enterprises. This assumption quickly proved ill-founded and, in 2005, the Council recommended the exclusion of several companies engaged in testing nuclear warheads and producing missiles solely designed to carry nuclear weapons. The list of products and activities leading to exclusion has subsequently become slightly longer, but they have in all cases concerned *warheads* and *missiles*. Even though the preparatory works were not very specific in this area, a consistent theme was that the threshold for the exclusion of companies should be high. To expand the grounds for exclusion to include strategic submarines and such vessels' component parts seems a long way from the situation envisaged in the preparatory works. Since the preparatory works are not very technical in their discussion of nuclear weapons, a normal understanding of the terms used there must be applied. In such an interpretation, it seems reasonable to assume that vessels and their constituent parts, irrespective of purpose or type, fall outside the normal understanding of the term *nuclear weapons and their key components*.

A more technical reason why the production of submarines should not be encompassed by the criterion is that they – from a purely physical point of view – are entirely separate from the nuclear weapon. A strategic submarine carries missiles,

which, in turn, carry nuclear warheads. Missiles and warheads (which do constitute grounds for exclusion) are physically bound together as a unit. The vessel is a separate entity, which is designed and built separately from the nuclear weapon. It is therefore not natural to equate the construction of ships with the production of nuclear weapons, ie missiles and warheads.

The report also argues that the proposed expansion of the grounds for exclusion will, over time, make it easier to practise and maintain the exclusion criterion in a consistent manner. However, the Council on Ethics doubts whether such a change would provide any operational benefits. It is true that the nuclear weapons criterion is difficult to apply consistently, but it is not primarily the submarine issue that is problematic. On the contrary, deciding not to exclude on this basis is an operationally simple matter. Changing the threshold for exclusion would probably increase

the number of doubtful cases. On the other hand, this does not constitute a weighty argument *against* expanding the criterion's area of application either. The proposed change would be operationally manageable for the Council, but can hardly be justified on the grounds that it would make application of the exclusion criterion easier.

Nor does it seem, despite a few exceptions, that other funds or investors who exclude companies on the grounds of nuclear weapons production routinely include delivery platforms in this practice.

#### **Further work**

With effect from January 2018, the Council on Ethics has entered into an agreement with a new supplier of screening services in the area of product-based exclusions. The Council will continue to apply the same delimitations with respect to the criteria as it has practised since 2005.



## Shipbreaking

Four shipping companies were excluded in 2017 because they had disposed of ships to be broken up for scrap on beaches in Bangladesh and Pakistan. This practice, known as *beaching*, is performed under extremely poor working conditions and causes significant environmental pollution. One company was placed under observation for its involvement in the same practice.

Large ships have a normal lifespan of around 25 years, after which their residual value lies in their scrap metal. For large ships, this amounts to anywhere between 5,000 and 40,000 tonnes of steel, whose recovery and reuse makes sense from both a financial and resource point of view, provided that it takes place in a safe and responsible manner. Globally, 1,000 to 1,200 large ships are broken up each year. Almost 80 per cent of the tonnage is broken up on the beaches of Bangladesh, India and Pakistan. The process involves running the vessel aground at high tide on beaches with a significant difference between the high and low-water mark, and then dismantling them *in situ*. Characteristic for beaching, as practised in Bangladesh and Pakistan, is the absence of the fixed installations or infrastructures that would be found at a quayside facility. Because the beached ships rest in sand or mud, access by crane or heavy machinery is not possible, so much of the work is performed manually. The ships are broken up by cutting off large sections which fall to the ground in the tidal zone. These sections are then dragged or carried ashore, where they are cut into smaller pieces and sold for scrap.

Also characteristic for the practice of beaching is that unskilled labourers carry out tasks that are extremely dangerous and hazardous to health, without training, protective equipment or basic safety precautions. The accident rate is extremely high, as are the health risks. In Bangladesh, the use of children to perform dangerous tasks has also been reported. Detailed information on the number of fatalities is not available. In Bangladesh, 1,000 to 2,000 fatal accidents have been reported since the 1990s, but the figures are uncertain. At least 30,000 people work directly in the shipbreaking sector in Bangladesh. In Pakistan, it is estimated that around 15,000 people are directly employed in shipbreaking. In recent years, there have been several major fires aboard ships that were being broken up in Pakistan, with the loss of many lives. How many people have also had their lives shortened as a result of injury or work that is hazardous to their health is difficult to estimate, but it is clearly a substantial number.

The Council on Ethics has attached importance to the continuous, innumerable and serious violations of a number of ILO conventions whose purpose it is to establish minimum standards which safeguard the lives and health of workers. The reported conditions demonstrate an almost total failure to comply with the conventions and to implement minimum standards, and this results in the vast number of accidents and considerable harm to health deriving from these operations. Indeed, one reason why it is possible to operate this business at a low cost is the deliberate use of minimal resources on measures such as protective equipment, training, safety procedures and creating a secure working environment. The Council considers that wide-ranging and serious violations of international health and safety conventions must be deemed to infringe fundamental rights to life and health, the sum of which must be said to constitute a serious breach of fundamental human rights.

In connection with *beaching*, the ships are normally run aground under their own power. They will therefore carry everything an operational vessel has on board, including fuel oil, lubricants and hydraulic oils; asbestos and PCBs. Their hulls are protected by anti-corrosion paint and anti-fouling coatings that may contain lead, cadmium, organic tin compounds, zinc and chromium. In addition, there are often remnants of the products the ship has carried. Without any form of infrastructure or facilities for the collection of pollutants, many of these substances will spill out into the natural environment, since it is not possible to collect waste and pollution that falls into the mud and is later washed out by the tides. In addition, environmental toxins and hazardous substances are able to disperse in an uncontrolled manner because parts are removed from the ships and sold on for reuse.

Environmental damage occurs as a result of failure to comply with both the Basel Convention and national legislation, in that several thousand tonnes of hazardous waste are sent annually to a country that has no infrastructure capable of dealing with it in a safe and sustainable manner. It is precisely this kind of transboundary transport of waste that the

convention is intended to prevent. Given that it nevertheless does take place, the consequences are predictable: Serious pollution and the dispersal of environmentally hazardous substances, which in turn have a negative impact on human health and ecosystems in the area. Although no comprehensive documentation exists with respect to the harm caused, studies have revealed levels of pollution including of heavy metals, that are excessively higher than establishes norms.

A report published by the World Bank in 2010 contains an estimate of the total volume of hazardous waste that will be transported to Bangladesh in connection with shipbreaking in the next 20 years, given that the current scale of the business is maintained. For Bangladesh, this will amount to an estimated 79,000 tonnes of asbestos and 240,000 tonnes of PCB. The country has no infrastructure or receiving apparatus to deal with this kind of waste.

There can scarcely be any doubt that, viewed in isolation, the environmental and working conditions associated with beaching as it is carried out in Bangladesh and Pakistan exceed the threshold for the exclusion of companies from the GPFG. However, these operations are not performed by companies in the GPFG's portfolio. Ownership of the vessel is normally transferred from the shipping company to a so-called cash buyer before it is broken up. When a company sells a ship to a cash buyer, it is at the outset clear that the ship is being sold for the sole purpose of scrapping. Furthermore, both parties are aware that the price agreed depends largely on two factors: the volume of steel in the ship and the cost of dismantling it. The cheapest method of dismantling a ship is by beaching, which is why this process gives the seller the highest price for the vessel concerned.

The Council on Ethics presumes that companies which dispose of ships for scrapping in this way

are fully aware of what will happen to them next. It must also be considered as general knowledge in the shipping industry that environmental and working conditions associated with beaching are extremely poor. That a ship is nevertheless sent for scrapping at the Chittagong beach in Bangladesh or the beaches at Gadani in Pakistan is a consequence of an active choice on the part of the company that owned the vessel to maximise its profit. In the Council's opinion, that company must shoulder an independent responsibility for doing so. There are better ways of dismantling ships that are readily available to the shipowner, but these are more expensive. In the opinion of the Council on Ethics, therefore, there exists a tangible connection between the shipowner's actions and the violation of ethical norms, which is of such a nature as to constitute a complicity under the GPFG's ethical guidelines.

The Council on Ethics has been in contact with a number of shipping companies in connection with its enquiries into this issue. The Council has taken as its starting point those companies which have disposed of several ships for beaching in Bangladesh and Pakistan during the past three years. Following the Council's approach, some companies have made it clear that they will no longer dispose of obsolete ships for the purpose of beaching. The Council has not recommended that these companies be excluded. One company has replied that it will strive to improve its practice in this area. The Council has recommended that this company be placed under observation. The Council has further recommended that those shipping companies which have given no indication of any such improvement be excluded from investment by the GPFG. The Council will re-examine the grounds for exclusion if at the end of four years the company has not sent any ships for *beaching*, or before that time if the company gives notice that it has ceased this practice.



# List of excluded companies by 1 March 2018

## Cluster Munitions

- General Dynamics Corporation
- Hanwha Corporation
- Poongsan Corporation
- Textron Inc.

## Nuclear Weapons

- AECOM
- Aerojet Rocketdyne Holdings Inc. (formerly GenCorp Inc.)
- Airbus Finance BV (formerly EADS Finance BV)
- Airbus SE (formerly EADS NV)
- BAE Systems
- Boeing Co./ The
- BWX Technologies Inc. (formerly Babcock & Wilcox Co.)
- Fluor Corp.
- Honeywell International Inc.
- Huntington Ingalls Industries Inc.
- Jacobs Engineering Group Inc.
- Lockheed Martin Corp.
- Northrop Grumman Corp.
- Orbital ATK Inc (after merger with Alliant Techsystems Inc.)
- Safran SA
- Serco Group Plc.

## Tobacco

- Alliance One International Inc.
- Altria Group Inc.
- British American Tobacco Malaysia Bhd.
- British American Tobacco Plc.
- Grupo Carso SAB de CV
- Gudang Garam Tbk. pt.
- Huabao International Holdings Ltd.
- Imperial Brands Plc.
- ITC Ltd.
- Japan Tobacco Inc.
- KT&G Corp.
- Philip Morris Int. Inc.
- Philip Morris Cr. AS
- Reynolds American Inc.
- Schweitzer-Mauduit International Inc.
- Shanghai Industrial Holdings Ltd.
- Souza Cruz Ltda.
- Swedish Match AB
- Universal Corp. VA
- Vector Group Ltd.

## Production of coal or coal-based energy

- Aboitiz Power Corp.
- AES Corp./VA
- AES Gener SA
- ALLETE Inc.
- Alliant Energy Corp.
- Ameren Corp.
- American Electric Power Co. Inc.
- Capital Power Corp.
- CESC Ltd.
- CEZ AS
- China Coal Energy Co. Ltd.
- China Power International Development Ltd.
- China Resources Power Holdings Co. Ltd.
- China Shenhua Energy Co. Ltd.
- Chugoku Electric Power Co. Inc./The
- CLP Holdings Ltd.
- Coal India Ltd.
- CONSOL Energy Inc.
- Datang International Power Generation Co. Ltd.
- DMCI Holdings Inc.
- Drax Group PLC
- DTE Energy Co.
- Dynegy Inc.
- E.CL SA
- Electric Power Development Co. Ltd.
- Electricity Generating PCL
- Emera Inc.
- Empire District Electric Co.
- Eneva SA
- Exxaro Resources Ltd.
- FirstEnergy Corp.
- Great Plains Energy Inc.
- Great River Energy
- Guangdong Electric Power Development Co. Ltd.
- Gujarat Mineral Development Corp. Ltd.
- HK Electric Investments & HK Electric Investments
- Hokkaido Electric Power Co. Inc.
- Hokuriku Electric Power Co.
- Huadian Electric Power Corp.
- Huadian Power International Corp. Ltd.
- Huaneng Power International Inc.
- IDACORP Inc.
- Inner Mongolia Yitai Coal Co. Ltd.
- Jastrzebska Spolka Weglowa SA
- Korea Electric Power Corp.
- Lubelski Wegiel Bogdanka SA
- Malakoff Corp. Bhd.
- MGE Energy Inc.

- New Hope Corp. Ltd.
- NRG Energy Inc.
- NTPC Ltd.
- Okinawa Electric Power Co. Inc./The
- Otter Tail Corp.
- Peabody Energy Corp.
- PGE Polska Grupa Energetyczna SA
- PNM Resources Inc.
- Public Power Corp. SA
- Reliance Infrastructure Ltd.
- Reliance Power Ltd.
- SDIC Power Holdings Co. Ltd.
- Shikoku Electric Power Co. Inc.
- Tata Power Co. Ltd.
- Tenaga Nasional Bhd.
- TransAlta Corp.
- WEC Energy Group Inc.
- Westar Energy Inc.
- Whitehaven Coal Ltd.
- Xcel Energy Inc.
- Yanzhou Coal Mining Co. Ltd.

#### Human Rights Violations

- Atal SA
- Wal-Mart Stores Inc.
- Wal-Mart de Mexico SA de CV
- Zuari Agro Chemicals Ltd.

#### Violations of the Rights of Individuals in Situations of War or Conflict

- Africa Israel Investments Ltd.
- Shikun & Binui Ltd.

#### Environmental Damage

- Bharat Heavy Electricals Ltd.
- Barrick Gold Corp.
- Duke Energy Corp. (including the below wholly-owned subsidiaries)
  - Duke Energy Carolinas LLC
  - Duke Energy Progress LLC
  - Progress Energy Inc.
- Freeport McMoRan Inc.
- Genting Bhd.
- IJM Corp. Bhd.
- MMC Norilsk Nickel PJSC
- POSCO
- Posco Daewoo Corp.
- Rio Tinto Plc.
- Rio Tinto Ltd.
- Ta Ann Holdings Bhd.
- Volcan Cia Minera SAA
- WTK Holdings Bhd.
- Zijin Mining Group Co. Ltd.

#### Human Rights Violations and Environmental Damage

- Evergreen Marine Corp. (Taiwan) Ltd.
- Korea Line Corp.
- Precious Shipping PCL

- Thoresen Thai Agencies PCL
- Vedanta Ltd. (previously called Sesa Sterlite, into which Madras Aluminium Company and Sterlite Industries Ltd. – both excluded 31 October 2007– were merged)
- Vedanta Resources Plc.

#### Corruption

- ZTE Corp.

#### Andre særlig grove brudd på grunnleggende etiske normer

- Cairn Energy Plc.
- Elbit Systems Ltd.
- Kosmos Energy Ltd.
- Potash Corp. of Saskatchewan
- San Leon Energy Plc.

---

## List of companies under observation as per 1. March 2018

#### Production of coal or coal-based energy

- CMS Energy Corp.
- EDP Energias de Portugal SA
- Endesa SA
- Glow Energy PCL
- Kyushu Electric Power Co Inc.
- NorthWestern Corp.
- OGE Energy Corp.
- Pinnacle West Capital Corp.
- Portland General Electric Company
- SCANA CORP
- Southern Co./The
- Talen Energy Corp.
- Tohoku Electric Power Co. Inc.

#### Environmental damage

- PT Astra International Tbk.

#### Environmental damage and human rights violations

- Pan Ocean Co Ltd.

#### Human rights violations

- Hansae Co. Ltd.
- Hansae Yes24 Holdings Co. Ltd

#### Corruption

- Leonardo SpA
- PetroChina Co. Ltd.
- Petroleo Brasileiro SA

An updated list can be found at <https://www.nbim.no/en/responsibility/exclusion-of-companies>





# Recommendations on exclusion and observation

---

# Published recommendations and observation letters

## Overview of recommendations published since the previous annual report

Company	Recommendation	Date published	Norges Bank's decision	Criterion
Bharat Heavy Electricals Ltd.	Exclusion	5 May 2017	Exclusion	Environment
PetroChina Co. Ltd.	Exclusion	5 May 2017	Observation	Corruption
Leonardo SpA	Exclusion	5 May 2017	Observation	Corruption
Eni SpA	Observation	5 May 2017	Active ownership	Corruption
Saipem SpA	Observation	5 May 2017	Active ownership	Corruption
Hansae Co. Ltd.	Exclusion	29 June 2017	Observation	Human rights
Hansae Yes24 Holdings Co. Ltd.	Exclusion	29 June 2017	Observation	Human rights
AECOM	Exclusion	16 January 2018	Exclusion	Nuclear weapons
Atal SA	Exclusion	16 January 2018	Exclusion	Human rights
BAE System Plc.	Exclusion	16 January 2018	Exclusion	Nuclear weapons
Evergreen Marine Corp. (Taiwan) Ltd.	Exclusion	16 January 2018	Exclusion	Environment and human rights
Fluor Corp.	Exclusion	16 January 2018	Exclusion	Nuclear weapons
Honeywell International Inc.	Exclusion maintained	16 January 2018	Exclusion maintained	Nuclear weapons
Huntington Ingalls Industries Inc.	Exclusion	16 January 2018	Exclusion	Nuclear weapons
Korea Line Corp.	Exclusion	16 January 2018	Exclusion	Environment and human rights
Pan Ocean Co. Ltd.	Observation	16 January 2018	Observation	Environment and human rights
Precious Shipping PCL	Exclusion	16 January 2018	Exclusion	Environment and human rights
Thoresen Thai Agencies PCL	Exclusion	16 January 2018	Exclusion	Environment and human rights

Since the previous annual report, 15 recommendations relating to a total of 18 companies have been published. Norges Bank has accepted the Council's recommendations relating to 12 of these companies.

The companies AECOM, BAE Systems Plc, Fluor Corp. and Huntington Ingalls Industries Inc. were excluded due to their involvement in the production of nuclear weapons. The Council on Ethics recommended that the exclusion of Honeywell International Inc. be maintained, but on different grounds. This company, too, was excluded on the grounds of nuclear weapons production.

The Council recommended the exclusion of PetroChina Co. Ltd. and Leonardo SpA because it considered that both companies had been involved in widespread and systematic corruption, while failing to implement adequate measures to prevent, uncover and deal with corruption in the future. In its assessment of future risk, emphasis was placed on the fact that the companies operate in countries and in business sectors in which the risk of corruption is high. However, Norges Bank deemed the companies' anti-corruption efforts to be sufficient to warrant placing them under observation for a period of time.

The Council also considered that the corrupt acts associated with Eni SpA and Saipem SpA were serious enough to qualify as gross corruption under the GPF's ethical guidelines, even though they were not as systematic and wide-ranging as those alleged to have been undertaken by PetroChina and Leonardo. The Council nevertheless recommended that Eni and Saipem be placed under observation because it considered that they had come further in the design of effective anti-corruption measures than the other two companies. However, Norges Bank concluded that the exercise of active ownership through Norges Bank Investment Management (NBIM) would be a more suitable approach to reducing the risk of future norm violations by these companies than observation.

The Council's recommendation to exclude the shipping companies Evergreen Marine Corp. (Taiwan) Ltd., Korea Line Corp, Precious Shipping PCL and Thoresen Thai Agencies PCL rests on the fact that they have, for several years, disposed of ships for scrap by sending them to be broken up on the beaches of Bangladesh and Pakistan. This process, called beaching, is carried out under extremely poor working conditions and causes substantial pollution. The Council considers that any company which disposes of ships for dismantling in this way can be said to contribute to gross human rights violations and serious environmental harm. The same grounds underpinned the recommendation to place Pan Ocean Co. Ltd. under observation. In contrast to the excluded companies,

Pan Ocean has indicated that it will discontinue its practice of disposing of ships to be broken up for scrap by beaching.

It was recommended that Bharat Heavy Electricals Ltd. be excluded because the company is building a coal-fired power plant extremely close to the boundary of the Sundarbans world heritage area in Bangladesh. Transport to and from the site will be carried out partly through the world heritage area, and extensive dredging of the watercourse, which is a vital part of the world heritage area, is planned. On the same grounds, the exclusion of the Indian company NTPC, which is the site operator, has previously been recommended.

The Council recommended that Hansae Yes24 Holdings Co. Ltd. and its subsidiary Hansae Co. Ltd. be excluded on the grounds of an unacceptable risk that they are responsible for systematic human rights violations within their own operations. Hansae Co. Ltd. owns textiles factories in Vietnam and elsewhere. The recommendation is based on investigations showing that the scale of norm violations has been extensive at several of the company's factories in Vietnam, that they have been going on for a long time, and that the company has not previously proved itself capable of implementing lasting improvements in working conditions. Norges Bank decided to place the companies under observation on the grounds that the measures they were in the process of implementing to improve working conditions provided a sufficient basis to warrant observing their progress in the time ahead.

Atal SA was excluded because it employs a subcontractor which has made use of workers from North Korea. In its recommendation, the Council attaches importance to several UN reports, which conclude that North Korean citizens who are sent abroad to work are the subjects of forced labour. The company has confirmed that there have been North Korean workers at its building project. The Council on Ethics considers that Atal has a responsibility for all the workers at its building sites, even though it is a subcontractor that is the direct contractual counterparty to the North Korean staffing agency which is the North Korean workers' actual employer. By accepting the use of North Korean workers, the Council considers that Atal contributes to gross human rights violations, including forced labour. Since the practice appears to be an accepted part of Atal's business model, the Council considers that the future risk of gross human rights violations is unacceptable.

## Summaries of recommendations published since the previous annual report.

### **Bharat Heavy Electricals Ltd.** **Submitted 8 December 2016**



The Council on Ethics recommends the exclusion of Bharat Heavy Electricals Ltd. (BHEL) from the Government Pension Fund Global (GPF) due to the unacceptable risk of the company being responsible for severe environmental damage through its operations in Khulna, Bangladesh.

BHEL has been awarded a contract to build a large coal-fired power plant in southern Bangladesh. The power plant is to be built close to the boundary of the Sundarbans national conservation area, the world's largest mangrove forest. The entire area is also a Ramsar area. It is rich in biodiversity and contains several protected species, including Bengal tigers and river dolphins. The conservation area also encompasses two world heritage sites in Bangladesh, as well as a further world heritage site on the Indian side of the border.

Two factors mean that the project carries a substantial risk of environmental damage. Transport to the power plant during the construction phase will mainly be by boat through the Sundarbans. The sailing route to the anchorage site passes very close to the boundary of a world heritage site. Transshipment and transport operations will raise the risk of mishaps and accidents involving emissions/discharges very close to vulnerable areas, and this risk is a direct consequence of the power plant and its location.

Another risk is linked to the fact that huge river-bed and seabed areas will be dredged. When large volumes are removed from the riverbed or dumped, the volume of particles transported by the currents increases substantially. There is a great risk that this activity may place further strain on the already endangered mangrove forest and life in the river and appurtenant marine areas, which are also important to the local population. At the same time, the river-bed conditions will change in protected areas for endangered river dolphins.

The Council on Ethics initially contacted BHEL on 19 May 2016. The company did not reply to the Council's inquiries initially, but has later submitted comments to a draft recommendation. The company states in the comments that there is no need to dredge the waterways.

The Council considers it highly unlikely that a coal-fired power plant can be built at this location without the construction work itself constituting a high risk of severe environmental damage, even if extensive new measures are implemented. In the present case, the company has also failed to sufficiently assess what needs to be done to protect the environment. Further, various transportation factors have not been addressed and handled satisfactorily. Overall, this indicates a significantly increased risk of unwanted incidents in a unique, highly vulnerable area. The Council has also given considerable weight to the strong concern expressed by UNESCO regarding the risks associated with the project and the fact that the IFC recommendations for such situations have not been followed. UNESCO has reviewed the project again in 2016 and calls for its cancellation or relocation.

### **PETROCHINA CO LTD.** **Submitted 8 December 2016**



The Council on Ethics recommends the exclusion of PetroChina from the GPF due to the risk of gross corruption.

PetroChina was established in 1999 and is listed on stock exchanges in New York, Shanghai and Hong Kong. It is China's largest producer and distributor of oil and gas, and plays a dominant role in China's oil and gas industry. The company has operations in 19 countries and a large number of subsidiaries.

The criterion of gross corruption encompasses active corruption, such as the payment of bribes in return for the award of contracts. However, the criterion also includes passive corruption, exemplified by the acceptance of bribes. The Council takes the position that, in the same way as active corruption, the widespread receipt of bribes is also an obstacle to social and economic development. It fosters discrimination, prevents social justice, distorts competition

and hinders sustainable economic development. In cases of passive corruption, the Council places particular emphasis on whether the practice seems to be widespread through the organisation and whether high-ranking employees are directly involved.

Around 65 former employees of PetroChina and employees in several of its subsidiaries are under investigation for allegedly accepting bribes, partly in return for awarding contracts to oil and gas subcontractors. In some of the cases, the allegations of corruption extend over the period from 1980 right up until 2014. All those who are assumed to be involved in corruption cases have held senior management positions in various divisions of PetroChina, as well as its subsidiaries. Of particular gravity, is the case against the man who served as PetroChina's CEO (2000–2013) and board chair (2007–2011). He has now been sentenced to 16 years in prison for having pocketed EUR 1.9 million in bribes from 14 sources between 2004 and 2013. In 2015, the *General Manager* of PetroChina Human Resources was sentenced to 20 years in jail for the receipt of EUR 6 million during the period 2000 to 2013. PetroChina's former *Executive Director* and its vice-chair up until 2015 is also under investigation for allegedly accepting bribes. The *General Manager* of *PetroChina Gas Utilization* was indicted for corruption in 2015, partly for having received bribes and for benefiting his family and friends to the tune of more than EUR 31 million. In addition, the former *General Manager* of PetroChina International Ltd, along with its former party secretary and vice president are thought to be under investigation for corruption, this latter for the receipt of bribes over a period of 22 years (1992–2014).

From November 2015 until July 2016, the Council on Ethics has engaged in a dialogue with PetroChina. The company has failed to provide much information on the matter, and has not submitted any comments on a draft recommendation. In its dialogue with the Council, PetroChina has not contested the corruption allegations. It has confirmed some cases, while claiming not to have relevant information relating to others. The Council on Ethics has attempted to arrange a meeting with the company in Beijing, but the company has responded that it prefers to pursue a written dialogue with the Council.

The oil and gas industry, as well as the construction industry, where large public contracts are common, exposes the company to the risk of corruption. In the Council's opinion, this places particular demands on the company to have robust systems in place and to implement measures that can effectively prevent, uncover and respond to corruption. Given that many of the company's former executives stand accused of gross corruption that is claimed to have taken place over a long period of time, this requirement becomes even more pressing. The onus is on the company to prove that it is working systematically and effectively to prevent corruption.

The Council notes that PetroChina has improved its internal corruption-prevention systems since 2014, and that numerous measures are currently being implemented in different parts of the company to prevent corruption. The Council nevertheless considers that the company has failed to provide sufficient information about the corruption-prevention measures now being implemented, nor has it substantiated how these will be function effectively throughout the organisation. This includes both the mapping and assessment of corruption risk, anti-corruption training, integrity due diligence of third parties, the whistleblowing system, performance monitoring and improvement.

In its assessment, the Council also points out that the company's management is largely the same today as when the corrupt practices are alleged to have taken place. Both the board of directors and group management are largely made up of people who have held senior positions with PetroChina and/or its parent company over many years, including when the corruption is alleged to have taken place. Management's attitudes are generally considered extremely important with respect to preventing corruption. In the view of the Council, when a company that has been involved in serious corruption cases does not purge management at all levels, but merely weeds out those actually convicted, it sends a signal that the company is not taking the necessary steps to prevent future non-compliances. The size of the amounts that are alleged to have been received in bribes also indicates that PetroChina's management knew, or should have known, about this practice.

In its assessment of future risk, the Council also attaches importance to the fact that the company has provided inadequate answers and failed to comment on its draft recommendation. In accordance with the remarks set out in Report No. 20 (2008–2009) to the Norwegian Storting (parliament), the Council on Ethics has, with respect to this case, accorded weight to the fact that deficient information about the company's conduct, and – not least – the company's lack of willingness to provide such information, may, in and of itself, contribute to the risk of becoming complicit in unethical behaviour being deemed unacceptably high.

The Council takes into account that the recent implementation of wide-ranging anti-corruption measures in China could play an important role in the prevention of corruption in Chinese companies. The Council on Ethics has nevertheless concluded that PetroChina should be excluded from the GPFG because it attaches greater importance to the corrupt practices already uncovered and the company's response thereto. Furthermore, the Council accords great weight to the measures the company has implemented to prevent corruption, seen in relation to the overall corruption risk in the same business sector and the same countries in which the company operates.

Based on the information available, the Council considers that there is an unacceptable risk that PetroChina may once again become involved in gross corruption.

## LEONARDO SPA Submitted 8 December 2016



The Council on Ethics recommends the exclusion of Leonardo SpA (Leonardo) from investment by the Norwegian Government Pension Fund Global (GPFG) due to the risk of gross corruption.

Leonardo, which is listed on the Milan Stock Exchange, employs some 47,000 people and is the largest industrial group in Italy. The company manufactures and sells aircraft, defence and security equipment primarily in Italy, the UK, the USA and Poland, though it also has operations in countries such as Turkey, Libya, Saudi Arabia, India, China and Russia.

The company is involved in corruption cases in four different countries. In April 2016, Leonardo's former board chair and CEO, the CEO of AugustaWestland, previously a subsidiary and now an integrated part of the Group, were sentenced to prison terms for gross corruption in connection with a helicopter contract in India. Several of the company's contracts for the sale of defence materiel are being investigated by the authorities in Italy, India, Algeria and South Korea. On the basis of the information available, it seems as though Leonardo's business partners and agents have forwarded bribes to public officials in these countries in order to secure contracts on behalf of the company right up until October 2014. Reference is also made to the fact that a further contract was annulled by Panama's Supreme Court in 2015 as a result of corruption allegations.

From October 2014 until September 2016, the Council on Ethics has engaged in a dialogue with Leonardo, both by means of written communications and in meetings. The company has provided information on the matter, and has also submitted its comments to a draft recommendation.

Leonardo has underlined that none of the allegations of corruption has been levelled at the company as such, and that all the facts relate to its previous management team. The Council on Ethics nevertheless presumes that in a company where senior management is involved in the circumvention of its own routines, there is reason to believe that the risk of non-compliance is substantial, and that more is required to alter the prevailing corporate culture than in companies where corruption occurs further down in the organisation and is more sporadic. The company's attitude towards the allegations gives the impression of an attempt to side-step its corporate responsibilities.

The Council on Ethics makes no assessment with respect to criminal liability, but attaches importance to whether internal rules and guidelines seem to have been broken, and whether there therefore exists a risk of corruption. On the basis of what is now known about the alleged incidents of corruption, the Council considers that previous internal systems must have failed.

The Council on Ethics notes that, in 2013, Leonardo made substantial changes in its board of directors and group management following the discovery of widespread corruption. In 2013, the board also set up a committee of experts to offer advice on how internal control systems and the anti-corruption programme could be improved. In light of this, it was to be expected that the company, within a reasonable period of time, would implement anti-corruption measures in line with international standards for best practice in the area. However, at the same time as the company set up its

external committee, it seems as though agreements continued to be entered into in violation of internal guidelines, for example by not performing sufficiently thorough *due diligence* investigations.

Leonardo operates in a number of countries in which the risk of corruption is high. For example, international indexes rank Libya, Russia and China in the highest category with regard to the presumed risk of corruption. The defence sector, where major public contracts are common and, furthermore, the subject of strict secrecy, also exposes the company to a further corruption risks. An important element in an anti-corruption programme is the continuous mapping of corruption risks. The company performed a wide-ranging assessment of all risks in 2015, but has not documented to the Council's satisfaction that it has a system whereby corruption risk is evaluated internally on a regular basis and effectively counteracted.

Leonardo uses agents in connection with public tenders in many countries, and they are rewarded with so-called success bonuses. The Council considers that the relatively extensive use of agents constitutes the largest corruption risk in the company's operations. The company says that it performs extensive due diligence assessments of third parties. Nevertheless, in 2015 it became known that one of the company's agents was supposed to have bribed a public official in South Korea, without the company's systems having picked up on this. The company states that it will now address this risk by incentivising its employees to use agents to a lesser extent than before. In the Council's view, the heralded scaling back in the use of agents is, in principle, important, but it nevertheless finds it difficult to attach importance to it because there are no specific plans for how and when this reduction will be achieved, or what the final target will be. Furthermore, it seems as though this should have been addressed as soon as the corruption allegations became known several years ago. All the incidents of alleged corruption involve agents. The Council also considers it to be a clear failing in the anti-corruption programmes that agents are not given anti-corruption training. This should be an important part of the preventive efforts made by the company, and is indeed given priority in other companies that are comparable with Leonardo.

In 2015, Leonardo established whistleblowing channels which employees are encouraged to use to report non-compliances. In its dialogue with the Council, the company has stated that it has never been alerted to corruption in its operations. Seen in light of the corruption profile a company like Leonardo has, the absence of such reports could be a sign that its anti-corruption efforts are not well enough communicated down through the organisation, that employees are not adequately encouraged to report their concerns, and that the systems do not function as they should.

Since Leonardo is involved in cases involving serious allegations of corruption which is supposed to have continued up until fairly recently, since the company continues to operate in countries with an extremely high risk of corruption without, at the same time, having adequately substantiated that it is working effectively to prevent non-compliances, the Council considers that there is an unacceptable risk that the company will once again become involved in gross corruption.

**ENI SPA**  
**Submitted 20 December 2016**



Due to the risk of gross corruption, the Council on Ethics recommends that Eni SpA be placed under observation.

Eni SpA (Eni) is an Italian energy company. Its operations encompass exploration for and the extraction and production of oil and gas, as well as their transport and refining. Eni has operations in 66 countries. As at 31 December 2015, Eni had 245 subsidiaries and 53 *associates, joint ventures and joint operations*, and employed 29,000 people.

In 2010, Eni and its two former subsidiaries, Snamprogetti and Saipem, entered into so-called *Deferred Prosecution Agreement* with the US Department of Justice with respect to bribes paid over the course of a decade in Nigeria



by a joint venture in which Snamprogetti participated. At the same time as this agreement was entered into, Eni was negotiating a high-value contract in Nigeria, to which suspicions of corruption are now being linked by the prosecuting authorities in Italy and Nigeria. In 2007 and 2010, Eni was engaged in negotiations with a company which, according to Eni's own risk assessments, was even in 2007 probably owned by a former Nigerian minister of petroleum. In 2007, he was sentenced in France to three years imprisonment for money laundering, and was ordered by a French appeal court in 2009 to pay a EUR 8 million fine in connection with the same offence. The case in Algeria relates to bribes that Eni's former subsidiary Saipem is supposed to have paid between 2006 and 2010.

From June 2015 until October 2016, the Council of Ethics has engaged in a dialogue with Eni, both through written communications and in meetings. The company has contributed information relating to these matters and has also commented on a draft recommendation. In its dialogue with the Council, Eni has underlined that the company has not been found guilty of any of the corruption charges.

The Council on Ethics makes no assessment of criminal liability. However, on the basis of that which is now known about all the corruption allegations, the Council believes that previous internal systems seem to have failed, and that defects in the company's internal control systems seem to have allowed corruption to have taken place within the organisation.

Eni operates in a number of countries where the risk of corruption is high. For example, according to *Transparency International's Corruption Perception Index, 2015*, Angola, Libya, Iraq, Venezuela, Nigeria, the Republic of Congo, Russia and Kazakhstan are all in the highest category with respect to the assumed risk of corruption. The oil and gas industry, as well as the construction industry, where large public contracts are common, also exposes the company to the risk of corruption. In the Council's opinion, this places particular demands on the company to have robust systems in place and to implement measures that can effectively prevent, uncover and respond to corruption. With several of the company's current and former leaders standing accused of gross corruption which allegedly took place in many countries, this requirement is even more pressing.

The Council notes that Eni has improved its internal corruption prevention systems since 2009, and that a number of measures are today in place in many parts of the company to prevent corruption. However, the Council believes that, up to now, Eni has not substantiated that its anti-corruption programme will be implemented effectively throughout its operations. This relates particularly to the "tone from the top", risk assessments and anti-corruption training. Reference is also made to the fact that one of the people now indicted in the Algeria case was promoted in 2014 to *Chief Upstream Officer* in Eni's group management, and that the company's former CEO is now also under indictment for corruption in Algeria. Finally, reference is made to the fact that the *Chief Development, Operations and Technology Officer* since 2014 and the former CEO are involved in the case in Nigeria relating to the acquisition of OPL-245. Irrespective of the outcome of these cases, the Council believes that these allegations make it difficult for group management to communicate a zero tolerance for corruption either internally or to its business partners.

However, the reason the Council is not recommending that the company be excluded, but instead be placed under observation, is that Eni has recently made organisational changes that more clearly allocate responsibility for compliance. The Council places particular emphasis on the *Integrated Compliance Department*, which will have complete responsibility for compliance, also in matters of anti-corruption. The company has given notice of several new measures, such as focal points in its non-listed subsidiaries, changes in the assessment of corruption risk and self-assessment of the efficacy of its classroom-based educational courses. Furthermore, the Council gives weight to the fact that Eni no longer has control of Saipem. The company's corruption risk therefore seems to have diminished. However, the Council acknowledges that several of these measures are new. What is crucial for an assessment of future risk is how they are implemented throughout the business.

In the coming two years, the Council will monitor developments in the corruption cases currently before the courts, as well as how the board enforces accountability on employees who are implicated in corruption in these and other cases which may be revealed, by means of the company's internal control systems, for example. The Council will also give weight to whether, in future, the board and group management establish and implement an anti-corruption programme that effectively prevents corruption. Should doubts be renewed about the degree to which management is taking responsibility for these matters, the criterion for exclusion may then be met.

**SAIPEM SPA**  
**Submitted 20 December 2016**



The Council on Ethics recommends that Saipem SpA be placed under observation due to the risk of gross corruption.

Saipem SpA (Saipem) is one of the world's largest oil service companies. It was founded in 1950 and was a wholly owned subsidiary of Eni up until 1984, when it was floated on the Milan Stock Exchange. The company employs 45,000 people and has operations in 70 countries.

Saipem is involved in several corruption cases in different countries around the world. The most serious and best documented case relates to corruption in Algeria between 2006 and 2010. Saipem is under indictment because, over several years, one of the company's agents is alleged to have paid out a total of USD 221 million in bribes to the Algerian company Sonatrach and to the country's former energy minister. In July 2016, a former senior executive was convicted on a guilty plea, and the company, along with a further three former senior executives, have been indicted in Italy in connection with the same offences. They are due to go on trial in December 2016.

From April 2014 until September 2016, the Council on Ethics has engaged in a dialogue with Saipem, both by means of written communication and in meetings. The company has contributed information in this matter, and has also commented on a draft recommendation. Saipem has underlined that its internal investigation of the allegations in Algeria concluded that Saipem has not paid bribes to public officials in Algeria, which is a precondition for criminal liability in this case, under national and US law.

The Council on Ethics makes no assessment with respect to criminal liability, but attaches importance to whether internal rules and guidelines seem to have been broken, and whether there therefore exists a risk of corruption. On the basis of what is now known about the case in Algeria, the Council considers that previous internal systems seem to have failed, and that defective internal control systems seem to have allowed corruption to take place in Algeria over several years.

Saipem operates in many countries where the risk of corruption is deemed high, according to international indexes. The oil and gas industry, as well as the construction industry, where large public contracts are common, also exposes the company to the risk of corruption. The company must constantly submit new tenders, and depends on a large number of suppliers. Finding equipment suppliers and subcontractors for construction work is a challenging process, which presumes that the company has complete control over its own employees. In the Council's opinion, this places particular demands on the company to have robust systems in place and to implement measures that can effectively prevent, uncover and respond to corruption. The onus is on Saipem to prove that it is working systematically and effectively to prevent corruption.

As far as the Council understands, Saipem took decisive steps in 2013 to implement important rules and routines, as well as organisational corruption prevention structures. The company has also made substantial changes in its board and group management after widespread corruption in the organisation was uncovered in 2013. This in itself may signal a new direction. The company also implemented relatively extensive preventive measures immediately after the Algeria case was uncovered in 2013. Moreover, the corruption investigations have had direct consequences for employees involved therein. No member of Saipem's current group management team or anyone now employed elsewhere in the company is implicated in the ongoing investigations.

Nevertheless, on the basis of the written information presented and after conversations with the company, the Council does not consider that Saipem has adequately substantiated that its present anti-corruption programme will effectively prevent corruption in the future. This rests on several grounds, including the company's assessment of its corruption risk and the reporting of presumed non-compliances. However, the reason the Council is not recommending that the company be excluded, but instead be placed under observation, is that the Council is uncertain whether further notified measures will be sufficient to reduce the risk of repeat offences. Saipem has relatively recently taken several

steps in the right direction. Here, the Council has attached importance to the probability that internal controls will be improved moving forward. The company is considering the establishment of an independent body which will take complete responsibility for compliance, including the anti-corruption programme. This may remedy several of the apparent defects in its preventive efforts. Here, too, the Council has accorded weight to the fact that an external consultant has been engaged to identify any weaknesses in the implementation of the existing anti-corruption programme in the most important subsidiaries and where the risk of corruption is, in all probability, greatest. The consultant will also offer advice on any need for improvement.

The Council is of the opinion that it would be expedient to re-examine this case in a couple of years. The Council considers that a substantial and continuous effort is needed to alter Saipem's corporate culture and will, at the expiry of this period, look at which measures have been implemented to this end. Furthermore, the Council will consider the extent to which Saipem can document that it is systematically mapping and assessing its corruption risk, that its training and whistleblowing systems are sufficiently effective, that the company has a detailed plan for monitoring and improving its anti-corruption programme, and for the implementation thereof, and that its anti-corruption efforts have the clear support of Saipem's group management and the board of directors.

**HANSAE YES24 HOLDINGS CO. LTD. OG HANSAE CO. LTD.**  
**Submitted 5 May 2017**



The Council on Ethics for the Government Pension Fund Global (GPF) recommends that Hansae Yes24 Holdings Co. Ltd. (Hansae Yes24) and its subsidiary Hansae Co. Ltd. (Hansae) be excluded from the GPF due to the working conditions at the latter's textile factories.

Hansae has 11 subsidiaries, which produce textiles and clothing in five countries in Southeast Asia. Hansae Yes24 is Hansae's largest shareholder and has a decisive influence over it. Both companies are listed on the stock exchange in South Korea.

The Council on Ethics has considered whether there is an unacceptable risk that HansaeYes24 and Hansae contribute to or are themselves responsible for systematic violations of internationally recognised human rights and labour rights.

To qualify as systematic, the human rights violations must be substantial in scope - that they are numerous in quantity, that different types of rights are infringed or that abuses take place in many entities within the company. The Council takes the position that "systematic" requires an accumulation of such violations and not merely isolated incidents; in other words that they constitute a pattern of behaviour. Furthermore, in its capacity as employer, each company has an individual and direct responsibility for its workforce and for preventing their employees' labour rights from being infringed at its own operations. The Council takes the position that, with respect to norm violations perpetrated within a company's own operations, the threshold for what can be accepted must be lower than when a company contributes to norm violations perpetrated by a third party.

In its assessment of the risk of further human rights violations, the Council attaches importance to how a company has responded when norm violations have been uncovered, and what it has done to prevent their reoccurrence.

This recommendation is based largely on reports deriving from inspections of working conditions at Hansae Vietnam's factories in the period October 2015 to October 2016, conducted by US organisations the Fair Labor Association (FLA) and the Worker Rights Consortium (WRC).

Numerous violations of statutory health and safety provisions were uncovered at Hansae Vietnam, including overwork leading to workers fainting at their sewing machines, restrictions on employees use of toilet facilities, as well as harassment, deficient fire safety precautions, forced overtime, illegal restrictions on sick leave, unfair dismissal, discrimi-

nation and a lack of freedom of association. These violations of ethical norms took place at several of Hansae Vietnam's factories, and also seem to be occurring at Hansae's subsidiary, Costec, in Myanmar.

Not all the violations can be characterised as human rights abuses and are not individually serious – but they are substantial in scope. They demonstrate that national laws are not being complied with, that measures are not implemented and that management makes little effort to verify and follow up that requirements relating to working conditions at the factories are met. The FLA found 81 violations of its guidelines, and has ordered Hansae Vietnam to implement around 250 measures via a "*corrective action plan*". According to the FLA report, Hansae Vietnam has already carried out many measures, with more scheduled for implementation in 2017.

Violation of labour rights at Hansae's operations has been pointed out over many years. Both individual customers and the Better Work Program regularly inspect the factories. For example, in several of its annual reports, Better Work has pointed out the lack of fire safety precautions and the lack of freedom of association. These conditions were nevertheless still observed by the WRC in 2016. The Council on Ethics concludes that, up to now, the company has not had a system in place to prevent, uncover and remedy violations of workers' rights.

The Council has communicated with Hansae on several occasions in the past year, and has also met with the company. Hansae Vietnam is in the process of remedying many of the norm violations uncovered during the inspections in 2016. Following its meeting with the Council on Ethics in September, Hansae has disclosed that it has put in place new management at Hansae Vietnam. The company has engaged a US law firm with experience in the field of human rights to evaluate the company's policies and initiatives, and to propose improvements to management systems and the implementation of best practices. The Council is also aware that Hansae has hired third-party expertise to help the company improve the dialogue between employees and factory management, and to provide training for Hansae Vietnam's management staff.

The Council on Ethics has noted that the company is now endeavouring to improve working conditions at Hansae Vietnam. Nevertheless, the Council attaches considerable weight to the fact that labour rights violations at the company have been pointed out for many years, and that Hansae has also previously pledged to correct norm violations in its own operations, without this resulting in lasting improvements. The Council considers that Hansae must create the necessary framework for a permanent improvement in working conditions, not merely at its factories in Vietnam, but in all its production facilities. This requires a significant change in attitudes to labour rights in the Group, as well as a comprehensive system through which the Group communicates that norm violations are unacceptable. It must also take responsibility for identifying risks, uncovering violations, addressing non-conformances and introducing a management system in which non-compliance with statutory provisions and internal guidelines has tangible consequences. It is not enough to respond piecemeal to norm violations at the individual factory only after they have been pointed out, as Hansae has done to date.

Even though Hansae is now prepared to make changes at other subsidiaries and factories as well, it is not clear to the Council how or when this will take place. A change in corporate culture, leadership and organisation in areas that are not solely linked to profit will be demanding and will probably take a long time. In light of the fact that the company's efforts to take a more systematic approach to labour rights seem to be in their infancy, that the scale of the norm violations at several of the company's factories has been extensive and has persisted over a long period, and that the company has not previously proved itself capable of generating lasting improvements in working conditions, the Council on Ethics considers that there is still an unacceptable risk that Hansae will continue to be responsible for systematic violations of labour rights.

**AECOM**  
**Submitted 22 April 2016**



The Council on Ethics recommends excluding AECOM from the Government Pension Fund Global (GPF) due to this company's involvement in the production of key components of nuclear weapons.

The basis for the recommendation is the company's central role in the activities at government facilities for the development, testing, maintenance and storage of nuclear war heads. In line with previous practice, the Council considers that such activities constitute production of nuclear weapons and thus grounds for excluding the company from the GPF.

**ATAL SA**  
**Submitted 25 August 2017**



The Council on Ethics recommends that Atal SA (Atal) be excluded from the Government Pension Fund Global due to an unacceptable risk that the company contributes to serious human rights violations. Atal is a Polish property development company. The company employs a subcontractor which has used North Korean workers at Atal's construction sites.

The Council bases its decision on several separate reports that show the situation for North Korean workers abroad to be of such a nature as to be deemed forced labour. Two elements must exist for a working situation to constitute forced labour – that a person is put to work involuntarily, and that the work is performed under the menace of a penalty. The involuntary aspect consists of the workers being sent abroad by the regime to a work situation of which they know nothing. Nor can they choose to cease working, since they have had their passports and mobile phones confiscated, are under constant surveillance and must remain at their place of work or domicile. The work is performed under the menace of a penalty. They must continue to work under the threat that their families at home may otherwise be punished.

Atal has confirmed that there have been North Korean workers at its construction sites. The Council on Ethics considers that Atal has a responsibility for all the workers at its building sites, even though it is a subcontractor that is the direct contracting party with the North Korean staffing company which is the North Koreans' employer. The Council considers that, by accepting the use of North Korean workers, Atal is contributing to serious human rights violations, including forced labour.

The fact that this appears to be an accepted part of Atal's business practice makes the future risk of serious human rights violations unacceptable.

**BAE SYSTEMS PLC.**  
**Submitted 17 March 2016**



The Council on Ethics recommends excluding BAE Systems plc. (BAE) from the Government Pension Fund Global (GPF) due to the company's production of key components for nuclear weapons.

In 2015, BAE entered into an eight-year contract with US authorities to maintain and upgrade the US Trident and Minuteman III missiles. These are missiles whose only function is to carry nuclear warheads. The Council has previously found that the manufacturing, maintenance and upgrading of such missiles can be equated with the initial production of key components of nuclear weapons and thus form a basis for excluding a company from the GPF.

**FLUOR CORP., HUNTINGTON INGALLS INDUSTRIES INC.,  
HONEYWELL INTERNATIONAL INC.**  
**Submitted 22 April 2016**



The Council on Ethics recommends excluding Fluor Corp. (Fluor) and Huntington Ingalls Industries Inc. (HII) from the Government Pension Fund Global (GPF) due to these companies' production of key nuclear weapons components. The Council also recommends maintaining the exclusion of Honeywell International Inc. (Honeywell).

Savannah River Nuclear Solutions LLC (SRNS) is owned as a joint venture by Fluor, Newport News Nuclear Inc. (NNN) and Honeywell International Inc. NNN is a wholly owned subsidiary of HII.

SRNS manufactures tritium, a radioactive isotope of hydrogen that is a key component in nuclear warheads. Tritium has a natural half-life of 12.3 years, which means it must constantly be recovered from helium-3 (a non-radioactive isotope of helium) to maintain the warheads' function. SRNS is the only manufacturer of tritium for this purpose in the USA and makes tritium solely in order to maintain the warheads' function. The Council has considered this activity to constitute production of key components of nuclear weapons.

In addition, the Council has noted that HII's wholly owned subsidiary, Newport News Nuclear Inc. (NNN), supplies special containers for the underground testing of nuclear weapons components at Los Alamos National Laboratory (LANL), and that Honeywell manufactures some nuclear weapons components at the state-owned Federal Manufacturing and Technologies (FM&T) in Missouri.



**EVERGREEN MARINE CORP. (TAIWAN) LTD.**  
**Submitted 29 June 2017**



The Council on Ethics recommends that Evergreen Marine Corp. (Taiwan) Ltd. (Evergreen Marine) be excluded from investment by the Government Pension Fund Global (GPF). Evergreen Marine is a Taiwanese company that primarily owns and operates container ships under the brand name Evergreen Line.

The Council rests its assessment on the fact that Evergreen Marine has for several years disposed of decommissioned vessels by sending them to be broken up for scrap on the beaches of Bangladesh and Pakistan, a practice known as beaching, where working conditions are extremely poor. The process also causes severe environmental damage. The Council considers that by disposing of ships for scrapping in this way, the company can be said to contribute to serious human rights violations and severe environmental damage. There are no indications that the company will cease disposing of ships by means of beaching.

The Council will re-examine the grounds for exclusion if at the end of four years the company has not sent any ships for beaching, or before that time if the company gives notice that it has ceased this practice.

**KOREA LINE CORP.**  
**Submitted 29 June 2017**



The Council on Ethics recommends that Korea Line Corporation (KLC) be excluded from investment by the Government Pension Fund Global (GPF). KLC is a South Korean company that owns and operates bulk carriers and LNG tankers.

The Council rests its assessment on the fact that KLC has for several years disposed of decommissioned vessels by sending them to be broken up for scrap on the beaches of Bangladesh and Pakistan, a practice known as beaching, where working conditions are extremely poor. The process also causes severe environmental damage. The Council considers that by disposing of ships for scrapping in this way, the company can be said to contribute to serious human rights violations and severe environmental damage. There are no indications that the company will cease disposing of ships by means of beaching.

The Council will re-examine the grounds for exclusion if at the end of four years the company has not sent any ships for beaching, or before that time if the company gives notice that it has ceased this practice.

**PAN OCEAN CO. LTD.**  
**Submitted 29 June 2017**



The Council on Ethics recommends that Pan Ocean Co. Ltd. be placed under observation. Pan Ocean is a South Korean shipping company that owns and operates bulk carriers, container ships and tankers.

The Council rests its assessment on the fact that Pan Ocean has disposed of obsolete vessels by sending them to be broken up for scrap on the beaches of Bangladesh, a practice known as beaching, where working conditions are extremely poor. The process also causes severe environmental damage. The Council considers that companies which dispose of ships for breakup in this way can be said to contribute to serious human rights violations and severe environmental damage.

In its assessment of the likelihood that the company will in future contribute to such norm violations, the Council on Ethics has attached importance to the company's assurance that it is willing in future to take the method of breakup into account as far as possible when making decisions on the sale of vessels for scrapping. Although the Council does not consider this to be a strongly binding pledge on the part of the company, it nevertheless perceives it as a positive indication of a change in future practice.

The Council will re-examine the grounds for observation if at the end of four years the company has not sent any ships for beaching, or before that time if the company issues a more binding pledge that it has ceased this practice. Should the company dispose of any more ships by means of beaching, the Council on Ethics will recommend that it be excluded from investment by the Government Pension Fund Global (GPF).

**PRECIOUS SHIPPING PCL**  
**Submitted 29 June 2017**



The Council on Ethics recommends that Precious Shipping PCL be excluded from investment by the Government Pension Fund Global (GPF). Precious Shipping PCL is a Thai company that primarily owns and operates bulk cargo vessels.

The Council rests its assessment on the fact that Precious Shipping PCL has for several years disposed of decommissioned vessels by sending them to be broken up for scrap on the beaches of Bangladesh and Pakistan, a practice known as beaching, where working conditions are extremely poor. The process also causes severe environmental damage. The Council considers that by disposing of ships for scrapping in this way, the company can be said to contribute to serious human rights violations and severe environmental damage. There are no indications that the company will cease disposing of ships by means of beaching.

The Council will re-examine the grounds for exclusion if at the end of four years the company has not sent any ships for beaching, or before that time if the company gives notice that it has ceased this practice.

**THORESEN THAI AGENCIES PCL**  
**Submitted 29 June 2017**



The Council on Ethics recommends that Thoresen Thai Agencies Public Company Limited (TTA) be excluded from investment by the Government Pension Fund Global (GPFG). TTA is a Thai shipping company that primarily owns and operates a fleet of bulk carriers.

The Council rests its assessment on the fact that TTA has for several years disposed of decommissioned vessels by sending them to be broken up for scrap on the beaches of Bangladesh, a practice known as beaching, where working conditions are extremely poor. The process also causes severe environmental damage. The Council considers that by disposing of ships for scrapping in this way, the company can be said to contribute to serious human rights violations and severe environmental damage. There are no indications that the company will cease disposing of ships by means of beaching.

The Council will re-examine the grounds for exclusion if at the end of four years the company has not sent any ships for beaching, or before that time if the company gives notice that it has ceased this practice.

Norges Bank, 14 March 2017

## The Council on Ethics' report to Norges Bank regarding its observation of Petróleo Brasileiro SA

In December 2015 The Council on Ethics recommended putting Petroleo Brasileiro SA (Petrobras) under observation due to the risk of gross corruption. Senior executives of the company and its most important suppliers had apparently for a decade organised a system of paying large bribes to top politicians, political parties and civil servants. Several of the company's senior executives also received large kickbacks. The Council did not believe that the company had proved it is effectively implementing its anti-corruption procedures, but nonetheless advised putting Petrobras under observation and not excluding it because the company's anti-corruption procedures were recently established. In addition, the extensive investigation in Brazil, the negative attention that the company had received both in Brazil and internationally and Brazil's new anti-corruption legislation all would reduce the risk of corruption reoccurring.

27 January 2016 Norges Bank decided to place Petrobras under observation and asked the Council on Ethics to monitor developments in this case. Throughout 2016, the Council has monitored how the company is working to develop and implement its anti-corruption programme. The Council has also observed how the company is dealing with investigations into past corruption, and has kept track of whether any new allegations of corruption have come to light.

The Council held meetings with Petrobras in October and December 2016 and in January 2017. The company has been given the opportunity to submit its comments on a draft of this report.

This is the Council's first annual report to Norges Bank with respect to this case.

### Key events since the recommendation was made in December 2015

The investigation of the corruption cases connected to Petrobras got underway in Brazil in 2014, but has continued at full strength in 2015 and 2016. According to Brazil's prosecuting authority, a total of 57 indictments have so far been brought against 260 separate people in the Lava Jato case.<sup>1</sup> So far, more than 100 businessmen, agents and politicians have been convicted of corruption in a court of first instance, including six former senior Petrobras executives, out of which five have also admitted corruption and signed plea agreements.<sup>2,3</sup> Another three former employees are charged with corruption. A number of multinational companies that have been engaged as suppliers to Petrobras are also under investigation and some have signed plea agreements admitting to corruption.<sup>4,5</sup>

Petrobras has put the value of its losses from corruption at an estimated USD 2 billion. Brazil's federal prosecution service, the *Ministério Público Federal* (MPF), has estimated the actual total loss to be far higher.<sup>6</sup>

The MPF, Brazil's Auditor General (*Controladoria-Geral da União*) and the Federal Court of Accounts (*Tribunal de Contas da União*) will continue to investigate the Lava Jato case.

---

1 As stated on the MPF's website, <http://lavajato.mpf.mp.br/atuacao-na-1a-instancia/resultados/a-lava-jato-em-numeros-1>.

2 Oglabo, <http://especiais.g1.globo.com/politica/2015/lava-jato/condenados-da-lava-jato/>

3 Email from Petrobras, 22 February 2017.

4 *Financial Times*, 15 February 2015, <http://www.ft.com/intl/cms/s/0/96152e80-b3ca-11e4-a6c1-00144feab7de.html>.

5 For instance Odebrecht, cf the American Department of Justice's webpage, <https://www.justice.gov/opa/pr/odebrecht-and-braskem-plead-guilty-and-agree-pay-least-35-billion-global-penalties-resolve>

6 *Financial Times*, 2 July 2015, <http://www.ft.com/intl/cms/s/0/3c937964-20d7-11e5-aa5a-398b2169cf79.html#axzz3kUSYdgpF>.

Petrobras is also under investigation for possible FCPA violations by the US *Department of Justice* (DoJ) and the *Securities and Exchange Commission* (SEC). The company has informed the Council on Ethics that its objective is to agree a settlement with the DoJ, but it remains uncertain when this may be possible.<sup>7</sup>

As a result of the corruption case in Brazil, legal proceedings have been brought against Petrobras in a New York court by a number of shareholders who are claiming damages for financial loss. In October 2016, Petrobras settled four separate lawsuits.<sup>8</sup>

According to information published in Brazilian and international media, Petrobras is also involved in cases of alleged corruption in several other countries, including Angola, Nigeria, Benin, Argentina and the USA. Several of these cases are under investigation in Brazil and the USA, but less information is available about them than the Lava Jato case.<sup>9</sup>

As stated in the Council's recommendation, Petrobras launched an internal inquiry in 2014, with the assistance of two external law firms. This inquiry is ongoing, though the company says it is uncertain when it will be concluded.<sup>10</sup> In its dialogue with the Council on Ethics, Petrobras has underlined that it is allocating considerable resources to this inquiry, and that, in 2015 and 2016, it initiated in-house investigations into a number of other cases of alleged corruption that have come to light partly through its specialized and independent whistleblowing channel.

In 2015, an independent committee, called the Special Committee, was set up to act as a reporting channel between the external law firms in charge of the external inquiry and the company's board. The committee has been given a broad and multi-faceted mandate to ensure, among other things, that the role played by company executives in the alleged corruption is "*investigated comprehensively*", so that the company will conduct its business in strict compliance with the regulations, adopt good practice with respect to corporate governance and strengthen its capability to prepare accurate financial reports to the stock exchange authorities. Furthermore, the committee will ensure that the company cooperates with all relevant investigative bodies. The *Special Committee* has been granted complete access to any criminal proceedings currently underway or concluded. The committee will ensure that the external investigators have sufficient autonomy and resources. It will evaluate periodic reports to the board and prosecuting authorities, and will assess and approve the external investigators' recommendations.<sup>11</sup>

### Changes in the board and group management

In addition to the comprehensive replacement of board members in 2014, Petrobras has made changes to its board and group management in both 2015 and 2016. In March 2015, the board's chair, a former Minister of Finance, stepped down.<sup>12</sup> Both the CEO and a director who had been a member of the board since 2008, resigned from the board in June 2016.<sup>13</sup> In May 2016, Brazilian media reported that one of those convicted in connection with the Lava Jato case had told investigators that both board members had been key players in the corruption system. The two are supposed to have come up with the plan for the illegal donation of funds to the ruling Labour Party, and illegal contributions to former president Dilma Rousseff's election campaign.<sup>14</sup>

---

7 Meeting between the Council on Ethics and Petrobras, 10 October 2016.

8 Reuters, 21 October 2016.

9 See for instance BBC Brasil em Londres 10 mai 2016: [http://www.bbc.com/portuguese/brasil/2016/05/160505\\_lavajato\\_exterior\\_tg](http://www.bbc.com/portuguese/brasil/2016/05/160505_lavajato_exterior_tg).

10 Meetings between the Council on Ethics and Petrobras, 10 October 2016 and 4 January 2017.

11 *Mandate and Charter of the Special Committee for the Internal Investigations of Petrobras*, 24 February 2015.

12 Bloomberg, 27 March 2015, <https://www.bloomberg.com/news/articles/2015-03-26/petrobras-names-coutinho-to-replace-mantega-as-chairman>.

13 SEC filing Form 6-K May 30 2016, [http://generate.api.edgar-online.com/EFX\\_dll/EdgarPro.dll?FetchFilingHTML?SessionID=9G-G6ezZedFjtG9\\_&ID=11417471](http://generate.api.edgar-online.com/EFX_dll/EdgarPro.dll?FetchFilingHTML?SessionID=9G-G6ezZedFjtG9_&ID=11417471).

14 Folha d S. Paulo May 8 2016, <http://www1.folha.uol.com.br/poder/2016/05/1769031-mantega-usou-bndes-para-pedir-doacao-diz-odebrecht.shtml>.

## The company's anti-corruption efforts since 2015

In its recommendation, the Council attached considerable importance to the fact that Petrobras had recently taken steps to establish an anti-corruption programme. The organisation of this compliance effort seemed to reflect international standards and best practice, and most of the initiatives were already in place in 2015. An independent anti-corruption department with sufficient authority and resources was established. The board also created the independent position of *Chief Governance, Risk and Compliance Officer (CGRCO)*. The incumbent of this position oversees the risk, corporate governance and compliance departments, and reports to the CEO, and in his capacity of a member of the *Special Committee*, to the board of Directors. He has veto rights over propositions of any other executive officer, and his contract can only be terminated with the agreement of a Board member appointed by the minority shareholders.

In 2016, the Council on Ethics met Petrobras's *CGRCO*, representatives of the *Compliance Area*, the legal affairs department, investor relations department, and the *Asset Manager* for Petrobras Nigeria (Upstream). In January 2017, the Council also held a meeting with a member of the *Special Committee*,<sup>15</sup> as well as the *CGRCO* and representatives of the *Compliance department*.

In its dialogue with the Council, the company has pointed out that its anti-corruption efforts have continued in 2016. Several changes have been made to the company's corporate governance model, including the way in which the board is appointed and organises its work. Qualification requirements, which also cover integrity and compliance, have been set with regard to board members. Furthermore, *CGRCO* now conducts thorough integrity inquiries into all board members and executives before they are appointed.<sup>16</sup> The length of time for which board members are appointed and the rules governing their reappointment have also been altered. It is, moreover, no longer possible for one and the same person to act as board chair and CEO.

Petrobras also set up several new board subcommittees in 2015 to ensure better corporate governance and control. It is now clear that the board has ultimate responsibility for compliance.

The compliance department currently employs more than 200 people. It is divided into three subunits, "*Internal Controls*", "*Compliance and Integrity Program*", and "*Internal Investigations*". 45 people work with internal control, 110 work with the anti-corruption programme and 42 work with internal investigations.

The Council has received a number of internal documents, including the *Compliance Department Report* to the board, guidelines and procedures for the implementation of anti-corruption activities and the compliance department's *Compliance Plan*, which also sets out detailed plans for internal control and anti-corruption activities in 2017 and 2018.<sup>17</sup> The Council on Ethics has also received a copy of the first set of recommendations made by the *Special Committee*, which the board approved in 2015, as well as a copy of a further set of recommendations from the *Special Committee* that were approved by the board in 2016. According to EY, which has been engaged by the board to monitor the implementation of the committee's recommendations, almost all of the first set of recommendations were implemented in 2015 and 2016.<sup>18</sup> The company aims to implement the additional recommendations as soon as possible.

Other improvements that the company says were implemented in 2016 include the fact that corruption risk is now assessed by the compliance department in conjunction with the risk department, internal auditing and other relevant bodies. On the basis of the company's *Corporate Risk Management Policy*, which was approved by the board in 2015, the *Compliance Area* drew up its own internal procedure for defining guidelines for the management of risk relating to fraud, corruption and money laundering. The aim is to reduce the company's risk exposure and to help identify, assess, manage and monitor these risks. According to the company's *Compliance Plan*, efforts to identify and manage corruption risk will be further refined and implemented in 2017.

---

15 Dr. Andreas Pohlmann.

16 Meeting between the Council on Ethics and Petrobras, 10 October 2016, and letter with attachments from Petrobras, 5 December 2016.

17 Letter to the Council on Ethics, with associated attachments, 5 December.

18 Summary of Status Report as of November 23, 2016, EY.



2016 also saw the development of specific training programmes for employees working in high-risk areas. During the year, face-to-face training has been given to employees working in procurement-related areas. The programme for classroom tuition will be further developed in 2017. On the basis of the feedback from employees, the existing online training programme, which has been taken by over 80 per cent of the group's entire workforce, will also be further developed in 2017. More time will be devoted to dilemma training and specific examples.

With regard to *integrity due diligence* on third parties, which also falls within the remit of the *Compliance department*, the company has introduced completely new procedures in 2016, which will be further refined in 2017.

In its dialogue with the Council, the company has also pointed to the appointment of a new *General Ombudsman* in 2016. This individual will receive all notices of rule violations and report directly to the board of directors. The company believes that this scheme has already produced positive results, namely that concerns are reported and logged systematically, cases are investigated and anonymous notices are handled in confidence. According to the *Compliance Unit Activities Report*, this has resulted in the receipt of over 1,000 reports of corruption and fraud in the period January to September 2016. During that same period, 61 disciplinary measures were handed out and 13 initiatives instigated. Employees have subsequently been fired and contracts with suppliers terminated as a result of the facts brought to light by internal inquiries.

According to the company's *Compliance Plan* for 2016, the compliance department intends to establish a system to monitor the efficacy of the anti-corruption programme in 2017. Work on this began in the summer of 2016.

According to the representative of the *Special Committee* that the Council on Ethics has spoken to, Petrobras has cooperated with relevant investigative bodies. Over a period of two years, the company has devoted substantial resources to uncovering corruption and reporting its findings to the authorities in both Brazil and the USA.<sup>19</sup> According to the CGRCO, the company has itself reported to the authorities several corruption cases that have been brought to light internally.<sup>20</sup> The *Special Committee* also considers that Petrobras has made many sweeping organisational changes, which will improve its internal controls. It also claims that much work has been done in both 2015 and 2016 to set up and implement an entirely new compliance programme. A number of relevant measures have already been implemented, while others will take some time to put in place. Although the Council on Ethics was told that Petrobras was "on the right track", it was also stated that the anti-corruption programme needed to be further developed and implemented in the coming years, and that the company must, in the longer term, assess its efficacy.<sup>21</sup>

However, it must be mentioned that in its dialogue with the company in 2016, it emerged that Petrobras was not fully implementing its anti-corruption programme in its international operations, for instance in that portion currently engaged in Nigeria. The company has maintained that it is working with BTG Pactual in a *joint venture* and that BTG also has responsibility for compliance. Furthermore, Petrobras has pointed out that its activity in Nigeria is insignificant, and that it is investing solely in projects there that Total and Chevron have operational responsibility for.<sup>22</sup>

### **The Council's assessment**

On the basis of the information which the Council on Ethics has received from Petrobras in 2016 and 2017, the Council deems the company to have substantiated that the anti-corruption efforts initiated in 2015 have continued in 2016, and that additional plans exist for the establishment and implementation of an effective anti-corruption programme. In particular, reference is made to the extensive written

---

19 Telephone conference between the Council on Ethics, Dr Andreas Pohlmann and Petrobras, 4 January 2017.

20 Meeting between the Council on Ethics and Petrobras, 10 October 2016.

21 Teleconference between the Council on Ethics, Dr Andreas Pohlmann and Petrobras, 4 January 2017.

22 Meetings between the Council on Ethics and Petrobras, 10 October 2016.

information that the Council received from Petrobras in December 2016, as well as the meeting with the *Special Committee* representative in January 2017. Access to information and documentation regarding measures the company has implemented has played an important role in the Council's decision to recommend continued observation rather than exclusion.

Nevertheless, the Council finds it challenging that the company maintains that it is merely the victim of the actions of individual former employees, and that the company as such is not responsible for what has happened. Given that the company has been accorded the position of aggrieved party in the criminal cases in Brazil and that civil litigation continues in the USA, where the issue of the company's culpability is key, this attitude is understandable. At the same time, the Council points to the allegations that have recently emerged in the Brazilian press implying that the person who chaired the company's board of directors until 2015 and a board member who resigned in 2016 may have played an important part in the corruption scheme. Furthermore, the Council is of the opinion that such an attitude on the part of management may discourage any changes in Petrobras's corporate culture and the effective implementation of the new anti-corruption programme.

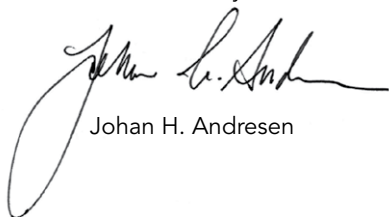
The Council notes that, in 2016, the company made changes to its articles of association which have improved its corporate governance model. Nevertheless, it remains the case that only one of the company's nine board members is elected by the non-controlling shareholders. It is therefore plausible to assume that the company's ability to avoid once again becoming involved in acts of corruption will depend on the measures being implemented to combat political corruption in the country.

Nevertheless, the Council does not find that Petrobras should be excluded from the fund. This assessment rests on several factors. One key factor is that substantial resources continue to be allocated to the uncovering of corruption, both through the use of external law firms and internal resources. Moreover, the company appears to be cooperating with prosecuting authorities in Brazil and the USA, and to be reporting to the authorities on corruption cases which are uncovered internally. The Council also attaches importance to the board's appointment of and mandate to the *Special Committee* and the *CGRCO*. The committee seems to have been an important prerequisite for the effective undertaking of internal inquiries, for structural changes in the internal control system and for the development of a renewed anti-corruption programme. The committee has also made recommendations for further improvement of internal controls, which the Council presumes will be followed up in 2017.

However, several of the company's former employees and a number of suppliers are still under investigation for corruption, and several more related investigations have been opened since the Council on Ethics issued its recommendation in 2015. What is important for the Council moving forward will be how the company responds to these cases, and whether it continues to develop its anti-corruption programme effectively in 2017. The Council will also attach importance to whether management clearly communicates a zero tolerance for corruption in the company, and creates suitable incentives to achieve this aim. In this, as in similar cases, the Council takes the position that the onus is on Petrobras to substantiate that it is working effectively enough to prevent, uncover and respond to corruption in its organisation.

The Council on Ethics will continue to observe Petrobras's anti-corruption efforts through ongoing dialogue with the company. The Council will also watch out for any information regarding cases of gross corruption in the company which may emerge through other channels, and will monitor the company's response to these.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'Johan H. Andresen', with a large, sweeping flourish at the end.

Johan H. Andresen



# **Guidelines for observation and exclusion from the Government Pension Fund Global**

---

### Guidelines for observation and exclusion from the Government Pension Fund Global

This translation is for informational purposes only. Legal authenticity remains with the original Norwegian version. The Norwegian version, *Retningslinjer for observasjon og utelukkelse fra Statens pensjonsfond utland*, can be found on lovdata.no. The Guidelines were last updated on 31 January 2017.

#### Section 1. Scope

(1) These guidelines apply to the work of the Council on Ethics for the Government Pension Fund Global (the Council on Ethics) and Norges Bank (the Bank) on the observation and exclusion of companies from the portfolio of the Government Pension Fund Global (the Fund) in accordance with the criteria in sections 2 and 3.

(2) The guidelines cover investments in the Fund's equity and fixed-income portfolios.

(3) The Council on Ethics makes recommendations to the Bank on the observation and exclusion of companies in the Fund's portfolio in accordance with the criteria in sections 2 and 3, and on the revocation of observation and exclusion decisions; cf. section 5(5) and section 6(6).

(4) The Bank makes decisions on the observation and exclusion of companies in the Fund's portfolio in accordance with the criteria in sections 2 and 3, and on the revocation of observation and exclusion decisions; cf. section 5(5) and section 6(6). The Bank may on its own initiative make decisions on observation and exclusion and on the revocation of such decisions; cf. section 2(2)–(4).

#### Section 2. Criteria for product-based observation and exclusion of companies

(1) The Fund shall not be invested in companies which themselves or through entities they control:

- a) produce weapons that violate fundamental humanitarian principles through their normal use
- b) produce tobacco
- c) sell weapons or military materiel to states that are subject to investment restrictions on government bonds as described in the management mandate for the Government Pension Fund Global, section 3–1(2)(c).

(2) Observation or exclusion may be decided for mining companies and power producers which themselves or through entities they control derive 30 per cent or more of their income from thermal coal or base 30 per cent or more of their operations on thermal coal.

(3) In assessments pursuant to subsection (2) above, in addition to the company's current share of income or activity from thermal coal, importance shall also be attached to forward-looking assessments, including any plans the company may have that will change the share of its business based on thermal coal and the share of its business based on renewable energy sources.

(4) Recommendations and decisions on exclusion of companies based on subsections (2) and (3) above shall not include green bonds issued by the company in question where such bonds are recognised through inclusion in specific indices for green bonds or are verified by a recognised third party.

#### Section 3. Criteria for conduct-based observation and exclusion of companies

Companies may be put under observation or be excluded if there is an unacceptable risk that the company contributes to or is responsible for:

- a) serious or systematic human rights violations, such as murder, torture, deprivation of liberty, forced labour and the worst forms of child labour
- b) serious violations of the rights of individuals in situations of war or conflict
- c) severe environmental damage
- d) acts or omissions that on an aggregate company level lead to unacceptable greenhouse gas emissions
- e) gross corruption
- f) other particularly serious violations of fundamental ethical norms.

#### Section 4. The Council on Ethics

(1) The Council on Ethics consists of five members appointed by the Ministry of Finance (the Ministry) after receiving a nomination from the Bank. The Ministry also appoints a chair and deputy chair after receiving a nomination from the Bank. The Bank's nomination shall be submitted to the Ministry no

---

## Guidelines

---

later than two months prior to the expiry of the appointment period.

(2) The composition of members shall ensure that the Council on Ethics possesses the required expertise to perform its functions as defined in these guidelines.

(3) Members of the Council on Ethics shall be appointed for a period of four years. Upon the initial appointment, the Ministry may adopt transitional provisions.

(4) The Ministry sets the remuneration of the members of the Council on Ethics and the Council on Ethics' budget.

(5) The Council on Ethics has its own secretariat, which administratively is under the Ministry. The Council on Ethics shall ensure that the secretariat has appropriate procedures and routines in place.

(6) The Council on Ethics shall prepare an annual operating plan, which shall be submitted to the Ministry. The operating plan shall describe the priorities set by the Council on Ethics for its work; cf. section 5.

(7) The Council on Ethics shall submit an annual report on its activities to the Ministry. This report shall be submitted no later than three months after the end of each calendar year.

(8) The Council on Ethics shall evaluate its work regularly.

### **Section 5. The work of the Council on Ethics on recommendations concerning observation and exclusion**

(1) The Council on Ethics shall continuously monitor the Fund's portfolio, cf. section 1(2), with the aim of identifying companies that contribute to or are responsible for production or conduct as mentioned in sections 2 and 3.

(2) The Council on Ethics may investigate matters on its own initiative or at the request of the Bank. The Council on Ethics shall develop and publish principles for the selection of companies for closer investigation. The Bank may adopt more detailed requirements relating to these principles.

(3) The Council on Ethics shall be free to gather the information it deems necessary, and shall ensure that each matter is thoroughly investigated before making a recommendation regarding observation, exclusion or revocation of such decisions.

(4) A company that is being considered for observation or exclusion shall be given an opportunity to present information and opinions to the Council on Ethics at an early stage of the process. In this context, the Council on Ethics shall clarify to the company what circumstances may form the basis for observation or exclusion. If the Council on Ethics decides to recommend observation or exclusion, its draft recommendation shall be presented to the company for comments; cf. section 7.

(5) The Council on Ethics shall regularly assess whether the basis for observation or exclusion still exists. In light of new information, the Council on Ethics may recommend that the Bank revoke an observation or exclusion decision.

(6) The Council on Ethics shall describe the grounds for its recommendations to the Bank; cf. sections 2 and 3. The Bank may adopt more detailed requirements relating to the form of such recommendations.

(7) The Council on Ethics shall publish its routines for the consideration of possible revocation of an observation or exclusion decision. Excluded companies shall be informed specifically of these routines.

### **Section 6. Norges Bank**

(1) The Bank shall make decisions on observation and exclusion in accordance with the criteria in sections 2 and 3 and on the revocation of such decisions, after receiving recommendations from the Council on Ethics. The Bank may on its own initiative make decisions on observation and exclusion in accordance with section 2(2)-(4) and on the revocation of such decisions.

(2) In assessing whether a company is to be excluded under section 3, the Bank may consider factors such as the probability of future norm violations, the severity and extent of the violations and the connection between the norm violation and the company in which the Fund is invested. The Bank may also consider the breadth of the company's operations and governance, including

## Guidelines

whether the company is doing what can reasonably be expected to reduce the risk of future norm violations within a reasonable time frame. Relevant factors in these assessments include the company's guidelines for, and work on, safeguarding good corporate governance, the environment and social conditions, and whether the company is making a positive contribution for those who are or have been affected by the company's conduct.

(3) Before making a decision on observation and exclusion in accordance with section 6(1), the Bank shall consider whether other measures, including the exercise of ownership rights, may be more suited to reduce the risk of continued norm violations, or whether such alternative measures may be more appropriate for other reasons. The Bank shall consider the full range of measures at its disposal and apply the measures in a coherent manner.

(4) Observation may be decided when there is doubt as to whether the conditions for exclusion are met or as to future developments, or where observation is deemed appropriate for other reasons.

(5) The Bank shall ensure that sufficient information is available before making a individual observation, exclusion or revocation decision.

(6) The Bank shall regularly assess whether the basis for observation or exclusion still exists

### **Section 7. Exchange of information and coordination between the Bank and the Council on Ethics**

(1) To help ensure the most coherent use of measures possible in the context of promoting responsible management, the Bank and the Council on Ethics shall meet regularly to exchange information and coordinate their work.

(2) Communication with companies shall be coordinated and aim to be perceived as consistent. The Bank shall exercise the Fund's ownership rights. The Bank shall seek to integrate the Council on Ethics' communication with companies into its general company follow-up. The Bank shall have access to the Council on Ethics' communication with companies, and may participate in meetings between the Council on Ethics and companies.

(3) The Council on Ethics may ask the Bank for information on matters concerning individual companies, including how specific companies

are dealt with in the context of the exercise of ownership rights. The Bank may request the Council on Ethics to make its assessments of individual companies available.

(4) The Bank and the Council on Ethics shall establish detailed procedures for the exchange of information and coordination to clarify responsibilities and promote productive communication and integration of the work of the Bank and the Council on Ethics.

### **Section 8. Publication**

(1) The Bank shall publish its decisions pursuant to these guidelines. Such public disclosure shall be in accordance with the management mandate for the Fund, section 6–2(4). When the Bank publishes its decisions, the Council on Ethics shall publish its recommendations. When the Bank on its own initiative makes decisions in accordance with section 6(1), the grounds for the decision shall be included in the publication.

(2) The Bank shall maintain a public list of companies excluded from the Fund or placed under observation pursuant to these guidelines.

### **Section 9. Meetings with the Ministry of Finance**

(1) The Ministry, the Bank and the Council on Ethics shall meet at least once a year. The information exchanged at such meetings shall be part of the basis for the reporting on responsible management included in the annual report to the Storting (the Norwegian parliament) on the management of the Fund.

(2) The Ministry and the Council on Ethics shall meet at least once a year. The following matters shall be discussed at the meetings:

- a) activities in the preceding year
- b) other matters reported by the Ministry and the Council on Ethics for further consideration.

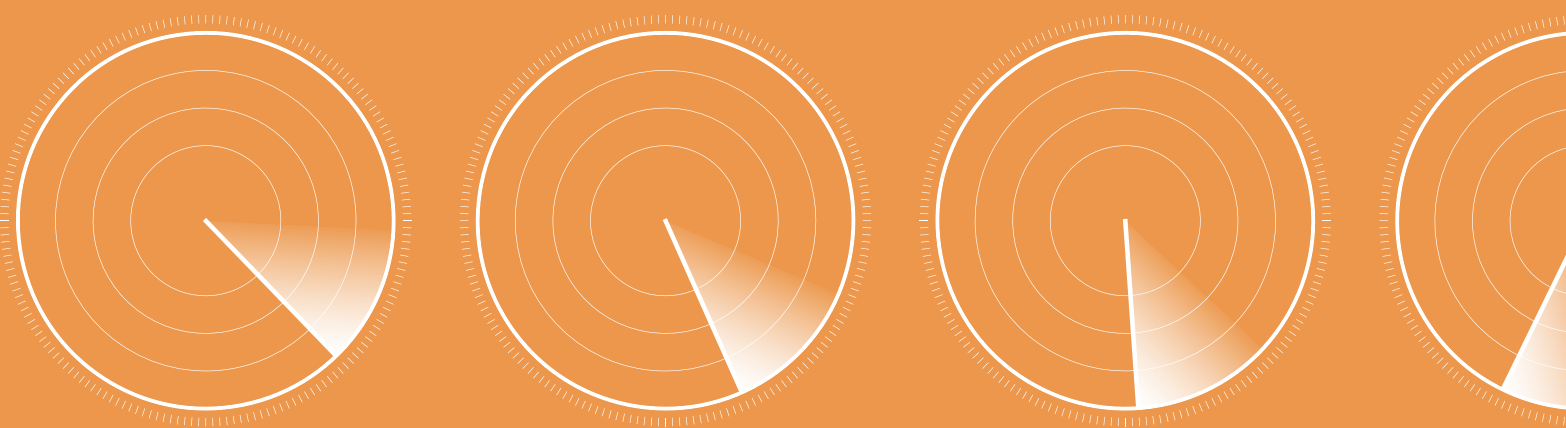
### **Section 10. Power of amendment**

The Ministry may supplement or amend these guidelines.

### **Section 11. Entry into force**

(...)







Council on Ethics for the Government Pension Fund Global  
Postboks 8008 Dep, N-0030 Oslo Norway

**[etikkradet.no](https://etikkradet.no)**