Natural Resource Governance Institute

Oil, gas and mining for development

Responding to the Challenge of Corruption in Resource-Rich Countries

Poor governance and systemic corruption are prevalent in many resource-rich countries. Given their highly concentrated and highly profitable nature, the oil, gas and mining industries can generate the kind of political and private incentives that favor rent-seeking and institutional (or state) capture.

In these resource-rich countries, other sectors of the economy, as well as the overall political class, tend to have close links to the extractives sector. Because of these linkages, weaknesses in governance and corruption do not remain confined to one sector. Rather, they are a nationwide development challenge.

As illustrated by Brazil's Petrobras scandal, high-level corruption in the extractive sector operates through sophisticated networks involving an influential and diverse range of players. The networks stretch across public, private and international spheres, and defy the traditional view of corruption as transactional bribery between two parties. Their members derive huge personal benefit from their ability to "capture" public resources, as well as regulatory and policy-making processes.

To identify pathways for addressing this challenge, multiple kinds of knowledge are required, and this information is often difficult to obtain. It is imperative to understand the politics of capture, and the make-up of the corruption networks – including their domestic and international dimensions. Moreover, this political understanding must be accompanied by an appreciation of the often-sophisticated processes through which corruption takes place. And the mechanisms of corruption adapt to and exploit the particular complexities and technicalities of the oil, gas and mining industries.

In this context, NRGI aims to provide evidence-based insight on corruption in the regions and countries in which we work. We have analyzed regional corruption trends in Latin America and Africa.[1] We have also produced research on individual loci of corruption, such the conduct of crude oil sales by the national oil company in Nigeria (see next page.) Our evidence-based approach benefits from data tools such as the Worldwide Governance Indicators (WGI), which help to illustrate the links between corruption and other dimensions of governance such as the rule of law. These data are inputs to our sector-specific Resource Governance Index (RGI), which measures the transparency and accountability of oil, gas and mining sector governance in 58 countries. Many of the indicators measured by the RGI – such as disclosure practices and the presence of checks and balances – constitute some of the recommended methods for fending off corruption risks.

In 2015, we at NRGI have begun to devote more resources to addressing corruption in resource-rich countries. Building on several regional and country analyses undertaken this year, our work in this area will pursue the following objectives:

1. Produce empirically grounded understandings of extractive sector corruption that draw on our sector expertise.
For example: to enable more systematic learning from real-world experience, NRGI will produce a library of 40 cases of oil, gas and mining sector corruption. The cases will focus mostly on license allocations, state-owned enterprises, and procurement (i.e., subcontracting). Along with a summary narrative, we will ask cross-cutting questions about each case – such as the role of middlemen or "fixers", or the presence of secret corporate vehicles. Analysis of the cases will produce stronger explanations for how corruption in the sector works, and a new source of evidence for multiple actors in the field.

2. Provide capacity building and technical assistance to the actors best-placed to identify and tackle corruption in resource-rich countries.
For example: NRGI will incorporate modules on corruption into its existing training courses for government officials, parliamentarians, journalists and civil society activists. The materials, tailored for the country or region in question, will provide concrete and actionable information about corruption patterns and risk points.

3. Advocate directly for home and host countries to prioritize addressing extractive sector corruption, including through global-level interventions.
In this area in particular, NRGI will prioritize working with corruption specialists within other NGOs, international organizations including the World Bank and OECD, academic experts, and others.

[1] Daniel Kaufmann, "Corruption Matters," *Finance & Development*, September 2015, pp. 20-23; and Daniel Kaufmann, "Evidence-Based Reflections on Natural Resource Governance and Corruption in Africa," *Africa at a Fork in the Road*, 2015, Yale Center for the Study of Globalization.

ILLUSTRATIONS OF OIL, GAS AND MINING SECTOR CORRUPTION

Corruption takes place in many countries, and at many points along the extractive industry decision chain.

DOMESTIC FOUNDATIONS FOR RESOURCE GOVERNANCE

Discovery and deciding to extract

Getting a good deal

Managing revenues

Investing for sustainable development

INTERNATIONAL FOUNDATIONS FOR RESOURCE GOVERNANCE

AIMROC

In 2007, the government of Azerbaijan awarded several 30-year mineral leases to AIMROC (Azerbaijan International Mineral Resources Operating Company Ltd.). One of the fields, the Chovdar gold field, holds an estimated $2.5 billion worth of gold. AIMROC is a joint venture between four firms, one of which is UK-registered Globex International, which held 11 percent of AIMROC. Globex was in turn owned by three companies in Panama, all of which, according to Panamanian registration records, list Leyla and Arzu Aliyeva, daughters of the president of Azerbaijan, as senior managers.[2]

Key challenges: Discretionary license allocation processes help politically exposed persons to participate in the mining sector; secret corporate vehicles in home countries including the UK enable the process.

Petrobras

In 2014, the Brazilian police began investigating $3.7 billion worth of suspicious payments as part of an elaborate bribery and kickback scheme whereby Petrobras officials funnelled money from colluding construction companies into political parties' coffers, while keeping large amounts themselves.[3] The scandal has shaken the confidence of Brazilians in their government institutions, and negatively impacted the economy.

Key challenges: Corruption networks spread across sectors, and undermine accountability within and outside of the oil sector; politicians can fuel corruption and gain advantages through the capture of key functions within public institutions.

NNPC revenue retention

Each year, Nigeria's national oil company discretionarily retains billions of dollars that should enter the treasury. For example, from 2005 to 2014, NNPC failed to transfer any revenues from an entire oil field's production – revenues worth over $12 billion. The company offers no public accounting, nor is it subject to any oversight, for how it spends the revenues.[4]

Key challenges: Extractive sector corruption is often systemic, with entire functions or institutions manipulated to serve narrow private interests, at the expense of the citizenry. This kind of abuse is more costly than simpler, transactional corruption, and is harder to prosecute.

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[2] Nushabe Fatullayeva and Khadija Ismayilova, "Azerbaijani Government Awarded Gold-Field Rights To President's Family", May 2012, *Radio Free Europe*.

[3] "The Big Oily: The Petrobras Scandal Explained", 23 January 2015, *The Economist*.

[4] Aaron Sayne, Alexandra Gillies and Christina Katsouris, "Inside NNPC Oil Sales: A Case for Reform in Nigeria", August 2015, Natural Resource Governance Institute.