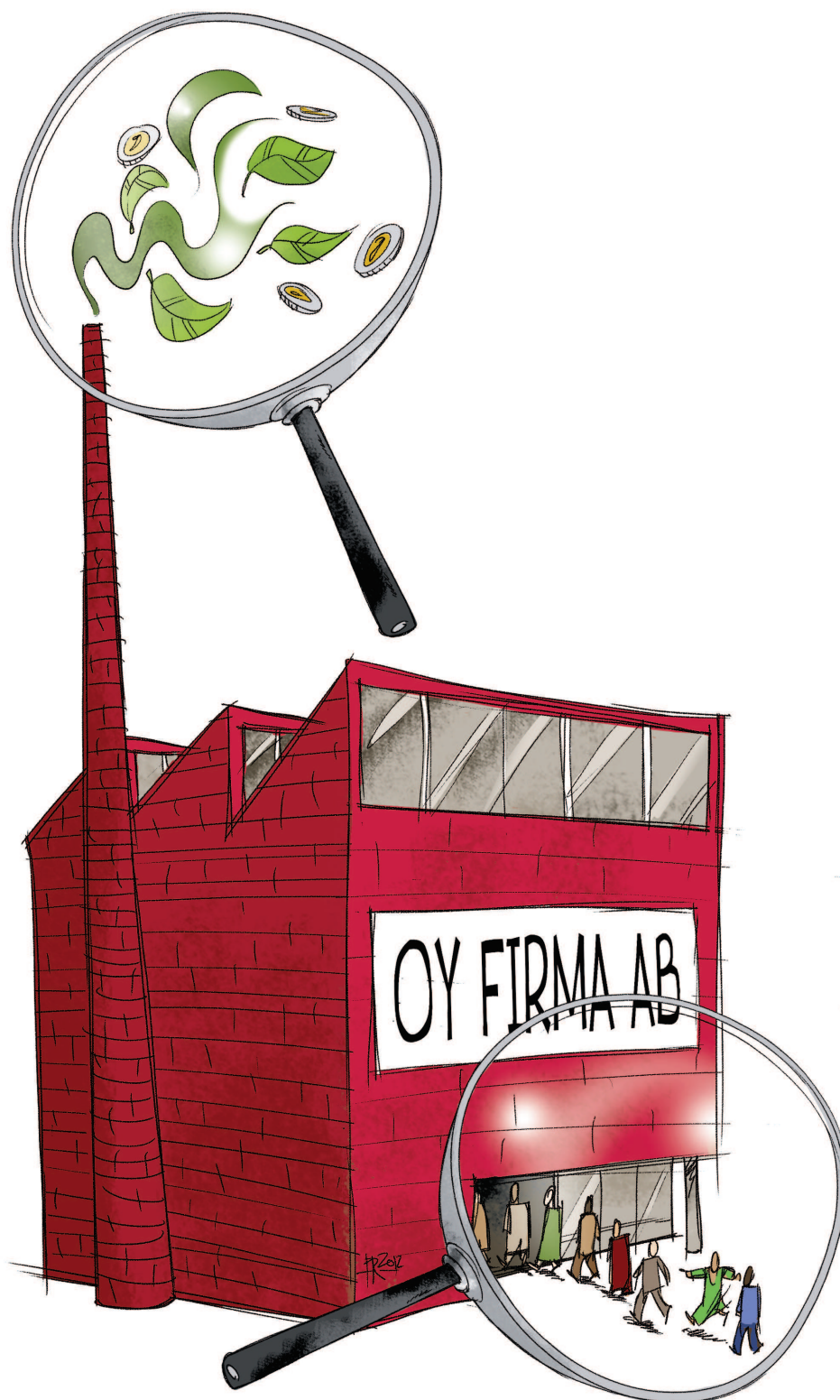


# CORPORATE ACCOUNTABILITY



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# CORPORATE ACCOUNTABILITY

WE SHOULD NOT BE INDIFFERENT TO THE WAY CORPORATIONS  
OPERATE IN DEVELOPING COUNTRIES.

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SHUTTERSTOCK

# CORPORATIONS UNDER SCRUTINY

CORPORATE ACCOUNTABILITY IS HARDLY A NEW ISSUE BUT IT IS BEING DISCUSSED NOW MORE THAN EVER. CORPORATE ACTIVITIES IMPACT AND BEAR RESPONSIBILITY FOR SOCIAL DEVELOPMENT.

► **ECONOMIC GLOBALISATION** and the recent economic crisis have sparked debate on distorted development and unethical corporate activity both in the North as well as the global South. Work has shifted from wealthy countries to countries of low cost production, and the causes of the economic crisis have been located in questionable private sector behaviour.

Investments in developing countries can bring advantages and disadvantages. Corporate activity can generate much-needed jobs, capital, technology, and know how for developing countries. And yet the rights abuses of workers and local inhabitants, environmental destruction, over-consumption of natural resources, tax evasion, and corruption are deplorably widespread.

## DEMANDING CORPORATE ACCOUNTABILITY

Europeans are obtaining increasingly more information about European corporations' operations abroad. There is more awareness about this thanks to such things as social media, increased travel and the work of Civil society organisations (CSOs). Concern about human rights violations, the use of child labour, and environmental

destruction crops up in informal chats and Facebook inputs.

The private sector now also occupies a central place in development cooperation. For instance, promoting corporate social responsibility is included as an objective in Finland's latest development policy programme. Including the private sector in negotiations between countries on development efforts has been taken up by, among others, the high-level forum on aid effectiveness, held in Busan, South Korea, in December 2011, and by the EU.<sup>1</sup> The hope is that the private sector will promote economic growth that will further development.

There are many opinions on the issue of corporate accountability. Views are divided, especially on whether such accountability should be voluntary or statutory. The private sector favours self-regulation, and assumes that the ethical choices made by consumers and investors progressively steer business operations towards accountability. So far, though, consumers' attitudes have had limited impact. The most profitable solution for companies is not always one that is socially or ethically sustainable. Problems arise above all when corpora-

<sup>1</sup> MFA (2012), OECD (2011), EC (2011)

tions operate in countries of high unemployment and weak democracy, and where there are gaps in occupational health and safety, and environmental legislation.

Many international organisations, such as United Nations (UN) and the International Labour Organisation (ILO) have policies and programmes designed to direct corporate activity, and different regions make use of their own standardisation systems. But there is little supervision of guidelines or principles, and no penalties for violating them. There is a need for more stringent national and international regulation, and more effective oversight of corporate accountability.

Civil society organizations and local associations may find themselves at loggerheads with corporations on issues of accountability. CSOs act as watchdogs of corporate accountability but engage in cooperation with businesses. Both roles are important. This report describes the impact of corporate activity in the global South. It tries to identify solutions to the problems associated with this activity. Here we chiefly focus on the corporate accountability of multinational companies. ◀

## WHAT IS CORPORATE ACCOUNTABILITY?

Discussion of corporate accountability often uses the concept of Corporate Social Responsibility (CSR), which came into use after the Second World War II, in particular in the United States.<sup>2</sup>

There is criticism of the CSR concept from a variety of perspectives. Already in the 1970s, supporters of the free market associated it with socialism.<sup>3</sup> Many CSOs, on the other hand, have seen it as simply corporate PR spin. Voluntary accountability has been labelled whitewashing or greenwashing. Greenwashing refers to superficial environmental accountability that extends no further than a company's image, while whitewashing relates to activity concerning social issues. The CSR concept has also been criticized because it emphasises social responsibility and pays scant attention to environmental responsibility.

### NO SINGLE DEFINITION

Just as there is a lack of consensus about what corporate accountability means in practice, no generally accepted definition of corporate accountability has emerged.<sup>4</sup> In addition to CSR, we find concepts that differ from one another to some extent, such as responsible business practice, responsible entrepreneurship, and corporate citizenship.

The subtext that such definitions have in common is that, in their operations, businesses should go beyond financial, technical and legal requirements. We also often find corporate accountability defined as a voluntary activity and a way to increase profits.<sup>5</sup> In this report we use the term corporate accountability. This means the accountability of corporations for the economic, social and environmental impacts of their activity. It means that a business is accountable to all stakeholders whom its operations affect. Accountable corporate activity is also resource and energy efficient.

When we talk of corporate accountability, we focus on the social impacts of core business operations, and not, for instance, on charity work done by businesses. Corporate accountability should not be based on volunteerism.

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<sup>2</sup> Howard R. Bowen gave one of the first definitions of corporate accountability in 1953. Bowen's view was that expectations placed on businesses generate a higher standard of living, economic growth and security, order, rights and freedom, and compliance with society's values. Bowen (1953).

<sup>3</sup> Friedman (1970)

<sup>4</sup> Joutsenvirta et al (2011)

<sup>5</sup> Carrol (1999)

# IMPACTS OF CORPORATE OPERATIONS ON THE GLOBAL SOUTH

DEVELOPING COUNTRIES ARE ENCOURAGED TO ATTRACT FOREIGN INVESTORS IN A VARIETY OF WAYS. IN THE WORST CASES, THE CARROT IS TAX BREAKS AND OTHER PERKS THAT DIMINISH THE INVESTMENT BENEFITS FOR THE COUNTRIES' DEVELOPMENT, AND TRAMPLE ON THE RIGHTS OF LOCAL COMMUNITIES.

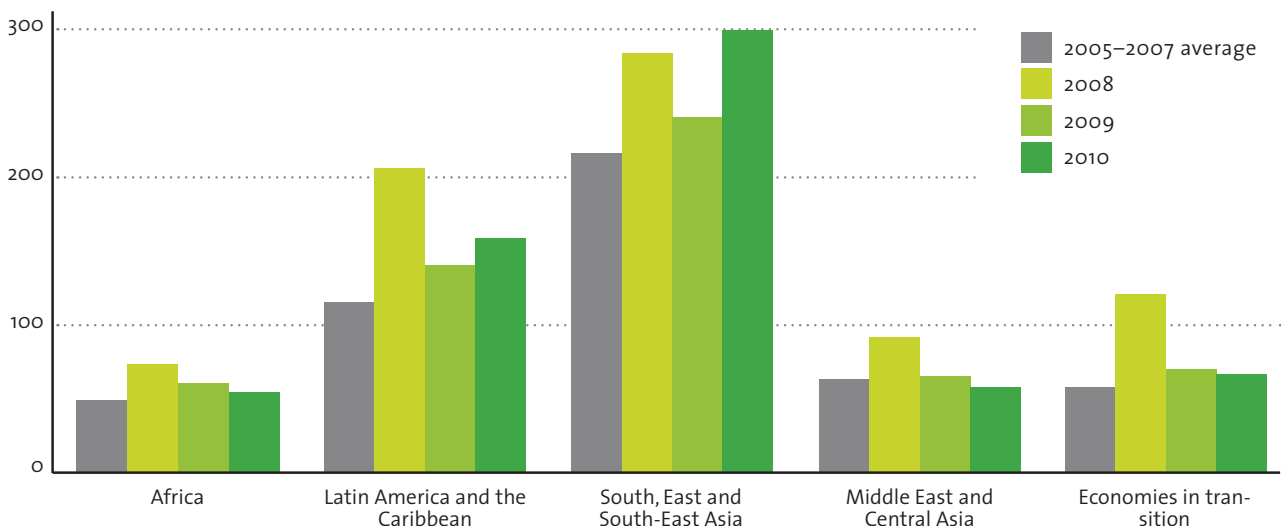
► **FOREIGN INVESTMENTS** in developing countries and emerging economies have been increasing for years, though subject to some recent decrease due to the economic crisis. Less than one per cent of investments by multinational corporations are directed at least developed countries, but their financial value is at almost the same level as the development aid these countries receive.<sup>6</sup>

With the globalization of production chains, companies have shifted production to areas where it is least

expensive. Also, developing countries have been encouraged, even pressured, to compete for foreign investments. Competition has led many countries to grant corporations various concessions and loosen the regulations they are subject to. Some countries have even set up free economic zones, where companies operate outside local regulations. Incentives aside, in many countries basic regulatory frameworks are from the outset inadequate, confused or else wholly unmonitored.

## DIRECT FOREIGN INVESTMENTS TO DEVELOPING COUNTRIES AND ECONOMIES IN TRANSITION

(billion dollars)



SOURCE: UNCTAD (2011)



This creates a bizarre situation where, in order to attract foreign investments to promote economic development, the benefits for developing countries are kept to a minimum. The results are tax evasion and avoidance, corruption, human rights violations, land grabs, and environmental crimes, and it is local people who suffer the consequences.

For decades, stakeholder thinking has been the usual way of looking at the relations of businesses with the surrounding society. But stakeholder identification has been deficient. Traditionally, key stakeholders are considered as being owners, clients, staff, consumers, subcontractors and suppliers. It is only in recent years that there has been a growing realisation that, in terms of corporate accountability, key stakeholders also include local communities, civil society organisations and the media.<sup>7</sup>

Companies have been accused of placing various stakeholders in a questionable order of importance. At the top are Western shareholders and global consumers, followed in second place by other Western stakeholders. Developing country citizens come last, and, due to their limited assets, they are not even included in the consumer bracket.<sup>8</sup> But taking them into account would be of primary importance for business operations to boost development. ◀

## MULTINATIONAL COMPANIES

Multinational companies by definition operate in many countries, with one country being their 'homeland'. They operate flexibly and are spread far and wide, and they often have an abstruse operating structure of subsidiaries and holding companies. Typically, multinational companies procure their products in part from subcontractors that they do not own.

There are nowadays an estimated 80,000 multinational companies, and they have about ten times that number of subsidiaries.<sup>9</sup> The number and size of multinational companies have mushroomed in the last few decades. Their turnover is bigger than the gross domestic product (GDP) of many states. The US chain Walmart is a good example of this. If Walmart were a state, its 2011 GDP would have been larger than 85% of countries.<sup>10</sup>

The emergence of multinational companies has changed world trade. Since the 1980s, most world trade has happened within multinational companies. So trade has not merely globalized but has become increasingly focused on the larger corporations that buy up smaller ones and merge with others.

6 The value of investments in least developed countries was \$US 26 billion in 2010, and the amount of development aid to least developed countries was \$US 27.2 billion in 2011. Source: UNCTAD (2011), OECD (2012).

7 Joutsenvirta et al. (2011)

8 Munshi and Kurian (2007)

9 Ruggie (2011)

10 Walmart (2010), IMF (2012)



## THE RIGHTS OF LOCAL COMMUNITIES

LOCAL COMMUNITIES ARE IMPORTANT CORPORATE STAKEHOLDERS IN THAT BUSINESS OPERATIONS VARIOUSLY AFFECT THE SURROUNDING COMMUNITY. COMPANIES NEED TO TAKE THE NEEDS OF LOCAL PEOPLE INTO ACCOUNT, AND RESPECT THEIR RIGHTS.

► **AT BEST** corporate investments provide local people with jobs and welfare. At worst, the opinions of locals are ignored, and a company destroys the environment or is guilty of land grabs, involving using lands that have been the source of subsistence for locals, sometimes for many generations.

There has been a massive increase in the scale of land grabs in recent decades. In the background is the food crisis of 2007-2008, plus the increase in resource consumption ensuing from the increased demand for land. Over the last decade an estimated 203 million hectares of land has been transferred from small farmers to foreign investors.<sup>11</sup>

The main perpetrators of land grabs are multinational agro, fuel, forestry and mining companies, or the financial developers, banks or pension funds that invest in them.

Unlike peaceful land purchasing or leasing, land grabs are associated with human rights abuses. They are not based on local consent, and there are often shortcomings in their impact assessments. Land grabs may also be linked to secret deals, which is why they violate the principles of good governance and democracy.<sup>12</sup>

For instance, the forestry sector impacts the lives of local communities in different parts of the world. Tree

plantations often prevent local people from using the land, and production causes greenhouse emissions. Another key sector that breaches the rights of local people is the mining and minerals industry. Mines require increasingly large areas of land for excavating ores, because many of the best deposits have been exhausted.<sup>13</sup>

It is not easy for companies to meet the expectations of all local communities. These may demand simultaneously the protection of land rights, new jobs and the minimization of environmental impacts. In impoverished and undemocratic areas, companies may even be asked to provide welfare services for local inhabitants.

But the provision of basic services should not remain the responsibility of companies, nor should corporate accountability in local communities be limited simply to charitable activity. Companies must ensure that their operations do not hamper the lives of locals or threaten their livelihoods, commit human rights violations or undermine good governance. The only way to identify the right ways of operating is to listen to the local population and take their views into consideration when planning and carrying out operations. ◀

<sup>11</sup> Anseuw et al. (2012)

<sup>12</sup> International Land Coalition (2011)

<sup>13</sup> Gaia Foundation (2012)

## CASE: WHO BENEFITS FROM THE LAND, AND ON WHAT TERMS?

NO ONE ASKS FOR THE OPINIONS OF LOCALS AND NOT ENOUGH COMPENSATION IS PAID WHEN THE TANZANIAN GOVERNMENT LEASES LARGE TRACTS OF LAND TO INTERNATIONAL COMPANIES.

► **THERE IS SUCH** a lot of unused arable land in Tanzania that there's also enough to meet the needs of international companies. This is what Tanzanian politicians claim. But because of complex rights and customs governing land use, it is hard to know whether or not local farmers are really using the land.

International companies whose operations are linked to agro-industry, biofuels or the REDD (reducing emissions from deforestation and forest degradation) funding mechanism may be granted 25-99 year leases from the Tanzanian Investment Centre of vast areas of land on which local people may depend for their livelihoods.

The impact assessments of company schemes are often inadequate. In 2005 the Swedish government-owned company SEKAB acquired 22,000 hectares of land in Bagamonyo area for a sugar plantation for producing bioethanol. At the preparatory stage of the scheme there was confusion when SEKAB was suspected of influencing the results of the environmental and social impact assessment.

The authorities' approval was based on the impact assessment report, from which SEKAB was suspected of deleting points it considered to be problematic. The area was not reckoned by the report to be prepared for such a large investment, and the project posed a threat to the area's water supply. SEKAB's Tanzanian operations later ended in bankruptcy, but the unused land has not been returned to local use.

### BENEFITS FOR LOCALS ON COMPANY CONDITIONS

In acquiring land mega investors operating in Tanzania pledge to hire local labour, produce quality welfare services, and generate new sources of income. The local population and the authorities are powerless to act when companies default on their promises.

The Norwegian company Green Resources acquired 20 000 hectares of grassland under the REDD mechanism for planting trees. The contract included service production for villagers, but on Green Resources' terms, and only the sale of emission allowances accumulated income.

It is often the case that the authorities approve contracts with foreign investors without listening to or even informing the local population. Compensation paid for land – if at all – is often below its market value. Companies take advantage of the structural weakness of Tanzanian rule of law at the expense of the environment and the local population. ◀

LINDA LÖNNQVIST  
KEPA TANSANIA

Land grabs make headlines  
every week in Tanzania

# COMPANIES, TRANSPARENCY AND DEMOCRACY

COMPANIES OFTEN CONCLUDE SECRET AGREEMENTS WITH STATES AND LOBBY FOR SPECIAL BENEFITS FOR THEMSELVES. GREATER TRANSPARENCY WOULD GIVE CITIZENS THE OPPORTUNITY TO MONITOR CORPORATE OPERATIONS AND DEMAND ACCOUNTABILITY.

► **DEMOCRACY, TRANSPARENCY**, good governance, good financial management, and a functioning infrastructure are important preconditions of a stable investment and business environment. In many countries these requirements have yet to be met.

Poor governance and secrecy limit the possibilities for citizens to track the activities of politicians and businesses, and, where appropriate, to require them to account for their actions. In Zambia, for example, secret mining agreements leaked and made public revealed that companies were granted exemptions that allowed them to disregard pension contributions, taxes and emission limits. For decades, the agreements had been kept secret from the trade union movement, members of parliament and even the regulatory authorities.<sup>14</sup>

Companies try to influence social decision-making at every stage in order to ensure an optimal operating environment for themselves. There is more lobbying of political decision-makers, especially in Europe and the US. In the US the private sector's trade association has sought to influence the preparation of the new Dodd-Frank Wall Street Reform and Consumer Protection Act with a total of 5,490 lobbyists.<sup>15</sup> The bill includes a provision for country-by-country reporting of financial performance by companies, aimed at bringing to light corporate corruption and tax evasion and

avoidance.

In Brussels the Corporate Europe Observatory recently revealed that multinational companies have even taken countries to court when their interests are threatened.<sup>16</sup>

## BRIBERY THRIVES ON POOR GOVERNANCE LOOPHOLES

Companies have also been implicated in cases of corruption. For example, the senior management of the listed Finnish engineering corporation Wärtsilä was charged with bribery concerning a power plant project in Kenya during 1999-2001. According to the prosecution, the company's director had paid bribes to Kenyan civil servants totalling EUR 3.4 million in order that the company would acquire the power plant project. The charges were later dropped.<sup>17</sup>

Giving bribes has no place among the methods available to an accountable company. Bribery is usually motivated by a desire to secure special benefits that reduce the cost of doing business. Increasing corporate transparency would improve the possibility for citizens to check that corporate activity brings benefits for the entire population instead of for the wrong people or only for a select few. ◀

# TAX EVASION IS COMMONPLACE

TAXATION IS A NEW ISSUE IN THE DISCUSSION OF CORPORATE ACCOUNTABILITY. IDEALLY, A RESPONSIBLE COMPANY PAYS ITS TAX AT THE POINT WHERE IT GENERATES TAXABLE INCOME, AND IS CANDID ABOUT ITS TAX PAYMENTS.

► **THE GLOBAL FINANCIAL INTEGRITY** think tank estimates that on average USD 725-810 billion a year flow from developing countries to the global North. Over half of capital flight is due to legal corporate tax avoidance.<sup>18</sup> The sum is massive compared to the roughly USD 105 billion development aid disbursed annually.<sup>19</sup> There are many reasons behind capital flight. First, transnational competition for foreign investments has led to companies being offered various tax benefits. One result of this is that companies only pay very little tax in developing countries, if at all.

Second, it is normal for business operations to try to minimise tax costs. In corporate-speak this is termed tax planning, otherwise known as tax avoidance. Companies set up subsidiaries in tax havens that engage in no actual business activity. The widespread network of subsidiaries of multinational companies allows for the transfer of profits within corporations to countries where tax levies are minimal. Tax haven companies are usually called holding companies, and their only task is to own subsidiaries and to collect the dividends that derive from them.<sup>20</sup>

14 Civil Society Trade Network of Zambia (2007)

15 The Economist (2012)

16 Gaia Foundation (2012)

17 Helsingin Sanomat (2009)

18 Global Financial Integrity (2011)

19 Figure for 2010

20 Kipa (2009)

The usual way to dodge taxation is to misapply transfer pricing by under or over pricing products. In under pricing products for export, a multinational company marks down prices in trading between subsidiary companies. In the target country the products are sold at market value. With over pricing, the same mechanism works the other way around. The remaining cash can then be invested in bank accounts in a country where there is intense banking secrecy.<sup>21</sup>

The actual value of goods for import or export can be made greater or lesser also by providing false information on their quality, classification or quantity. Companies may declare fictitious trade items, which are paid for even though the products are non-existent. The sums paid can thus be transferred from a country of strict taxation to a low tax environment.<sup>22</sup>

Tax evasion and avoidance is a special problem for developing countries because their tax revenues and equity ratio are already low, and they cannot afford

to produce essential basic services or infrastructure. Their tax revenue is anyway low because the informal economy is large and the capacity of citizens to pay tax is small. Developing countries are also under pressure to eliminate customs duties and other fees that limit the free flow of investments, which is why state income levels have declined even further.

The resources that the authorities have to monitor corporate tax payment are often poor, even in those developing countries that try to tax business operations. This is why there is an emphasis on accountability by companies operating in the global South.<sup>23</sup> Having fair tax revenues would increase the self-sufficiency of developing countries and reduce their dependence on development aid. As a first step towards this it would be important to increase transparency by requiring companies to publicise their financial records on a country-by-country basis (see page 20).◀

<sup>21</sup> Ibid.  
<sup>22</sup> Action Aid (2009)

<sup>23</sup> Ylönen and Simola (2011)

## CASE: CONTROVERSY IN MOZAMBIQUE OVER BENEFITS OF MEGA INVESTMENTS

MOZAMBIQUE HAS BEEN ABLE TO ATTRACT A NUMBER OF HUGE INVESTMENTS, SO CALLED MEGA PROJECTS. BUT THE DEVELOPMENT MODEL THEY DENOTE HAS BEEN UNDER CRITICISM. GDP IS INCREASING, BUT DOES ECONOMIC DEVELOPMENT EXTEND TO THE MOST VULNERABLE?

► **PARLIAMENT REQUESTED** the government to clarify how increased investments in the natural gas and coal industry is supporting the country's development and benefiting the people living in mining areas. The opposition says that project revenues have not improved the welfare of ordinary citizens. Civil society is also not convinced about the benefits of mega projects.

Mineral resources minister Esperança Bias argues that they do generate tax revenue. The minister also lauds their job creation and corporate social responsibility programmes. Government is also tightening up on taxing the utilization of natural resources, particularly in the forestry sector. In 2005, legislation came into effect under which 20% of income from logging should be returned to

local communities.

According to the government, income is already being used for such things as renovating schools and providing water points.

### PUTTING THE BRAKE ON TAX BREAKS

Civil society in Mozambique has criticised the secrecy of contracts between government and mega projects. The frontline organisation Centro de Integridade Pública has called for the agreements to be made public and for them to be re-negotiated. It is precisely such things as tax concessions that these secret agreements contain.

Even the International Monetary Fund (IMF) and the World Bank have focused on the tax concessions granted for Mozambique's mega projects. Only 5% of the state budget is covered by income from these projects.

According to an IMF report, there is no longer any justification for such dramatic tax breaks. The Fund proposes improvements to infrastructure and the diversification of the economy so that Mozambique would have an opportunity to substantially decrease dependence on aid.◀

The Mozambican government has promised tighter taxation of natural resource use



ISTOCKPHOTO

## WORK WITH DIGNITY

THOUSANDS OF FINNISH COMPANIES RUN OPERATIONS IN COUNTRIES IN WHICH LEGISLATION PROTECTING WORKERS' RIGHTS IS WEAK OR NOT MONITORED. RESPONSIBLE COMPANIES GUARANTEE THEIR EMPLOYEES' RIGHTS AND DECENT WAGES IN THESE COUNTRIES.

► **COMMON PROBLEMS** in many countries include having to live on insufficient pay and endure unreasonably long working days, and disregard for trade union rights. In the worst cases, workers in low cost production countries work for 80 hours a week on very low wages. In many the majority of them are women.<sup>24</sup> There is no pension accrual, and bad working conditions mean that there is a risk of not reaching retirement age.

The level of pay in developing countries is often so depressed that having work is not enough to lift people out of poverty. The globalisation of goods and service production is also evident in Finland, in addition to the global South: factories have been closed down, and in many companies remaining in Finland workers have been forced to accept substandard terms of employment in the name of being competitive.

International Labour Organisation (ILO) conventions enshrine workers' rights. Core ILO conventions concluded between 1930 and 1999 prohibit the use of forced and child labour, as well as workplace discrimination.

They also guarantee freedom of association, contractual rights, equal pay, and the minimum working age.<sup>25</sup>

A recent annual report of the International Trade Union Confederation (ITUC) nevertheless makes grim reading: in 2010, 90 people were murdered for belonging to trade unions, 75 had their lives threatened, 2 500 people were arrested, and 5,000 were sacked. Trade union activity has become increasingly difficult due to the global economic crisis. The report reveals that many countries do not implement employment related legislation at all. Female workers, especially, are in an extremely bad situation in free trade zones around the world.<sup>26</sup>

In Finland too, workers' rights have been a persistent theme of the debate on corporate accountability. Many reports reveal that a lot of Finnish firms buy their products from subcontractors that fail to guarantee workers decent wages or safe working conditions.<sup>27</sup> Companies must adhere to the ILO's international conventions, and pay employees fair wages. Subcontractors must also be held accountable over this. ◀

24 Clean Clothes Campaign (2006)

25 ILO (2012)

26 ITUC (2011)

27 Finnwatch and Clean Clothes Campaign (2010), Finnwatch (2011)

# CORPORATE ACCOUNTABILITY FOR ENVIRONMENT AND CLIMATE

KNOWLEDGE OF THE ENVIRONMENTAL PROBLEMS ASSOCIATED WITH CORPORATE OPERATIONS HAS BEEN AROUND FOR A LONG TIME, BUT IN MANY DEVELOPING COUNTRIES CORPORATIONS REAP BENEFITS FROM WEAK ENVIRONMENTAL LEGISLATION OR FROM ENVIRONMENTAL COMPLIANCE CONCESSIONS GRANTED TO THEM SEPARATELY.

► **AT BEST**, foreign investments introduce new environmental technology to developing countries that can help further their sustainable development. In many countries there is a need for improved technology for such things as wastewater treatment. But environmental technology is expensive, and companies aiming for the lowest possible production costs show little enthusiasm for investment in it.

Greenhouse gasses are the most common forms of environmental harm caused by corporate activity, together with pollution, waste and the destruction or over consumption of natural resources. The electricity, oil, gas, metals and mining sectors, as well as food production and construction sectors are the main ones responsible for this environmental harm.<sup>28</sup> Water usage by companies in areas with scarce groundwater can mean that local inhabitants have no access to clean drinking water.

## A PRICE TAG ON ENVIRONMENTAL DESTRUCTION

In corporate activity value is usually only attached to things that have a price. So-called ecosystem services – meaning air, water, and soil – have no price tag. The secretariat of the UN's Principles for Responsible Investment (UNPRI) estimates that if the 3,000 largest corporations in the world paid for their use and destruction of the environment, they would lose a third of their annual income – altogether USD 2.15 billion.<sup>29</sup>

Also, environmental destruction doesn't show up in countries' GDP. Both corporate activities that destroy the environment and those that minimise environmental impacts have the same effects on GDP. There is a need, alongside GDP, for new prosperity indicators that take better account of environmental and human welfare.

One well-known example of corporate environmental harm concerns the Niger Delta, which oil companies – especially Shell – have polluted since the 1960s. The natural environment of the Niger Delta is unique in its diversity: the area contains a mangrove forest, freshwater swamps and rainforest. The United Nations Development Programme (UNDP) estimates that 60% of the

region's population depend on the natural environment for their livelihood.<sup>30</sup> The oil spills and gas flares resulting from oil production have caused immense environmental destruction, and polluted the water and agricultural land.<sup>31</sup>

Allowing exceptions from environmental regulation is a way for developing countries to attract investors. The key issue with them is whether multinational companies operating in the South comply with the same environmental standards as they do in their own countries, and whether they demand the same of their subcontractors. For the heavily polluting mining sector this is especially applicable, because the rising price of raw materials has attracted increased investments in mining. In Zambia and Tanzania, for instance, over a fifth of investments are in mining, and their mineral mines are wholly under the control of foreign corporations.<sup>32</sup>

## PROFITS FROM THE CLIMATE CHANGE

In money terms greenhouse gas emissions are the main burden on the environment caused by corporations.<sup>33</sup> Corporations are the main cause of climate change. While efforts are being made to control corporate emissions, many companies have begun to make business out of climate change, for instance by producing biofuel. Companies need to be brought on-board concerning climate change, but related corporate activity in the South has many harmful repercussions, especially in terms of locals' land ownership rights. (See p. 8)

Land grabs linked to biofuels account for up to 66 per cent of African and 50 per cent of Asian land acquisitions.<sup>34</sup> The climate business also affects food prices. The US and the EU have devoted public funds to support biofuel production, with the result that maize suitable for biofuel takes up land space from wheat farmers. And so world wheat prices have increased.<sup>35</sup> European companies are central players on the biofuel market. One of the largest of them is Neste Oil, which produces fuel mainly from palm oil. In Indonesia palm oil production has devastated tropical rainforests. ◀

28 UNPRI (2011)  
29 Ibid. Figures for 2008.

30 UNDP (2006)

31 Amnesty International (2009)

32 Kepa (2007)

33 UNPRI (2011)

34 Schonveld (2011)

35 Kepa (2008)



## CASE: FINNISH LACK OF ACCOUNTABILITY AT MEKONG RIVER DAM SITE

LAOTIAN GOVERNMENT REPORT COMMISSIONED FROM THE FINNISH FIRM PÖYRY SUPPORTS DAM CONSTRUCTION THREATENING FISH SPECIES AND ECOSYSTEMS.

► **IN RECENT YEARS**, Laos has opened up to foreign investment concerning construction of the Xayaburi dam. In April 2011, plans for this, the country's first dam, on the mainstream of the lower Mekong River, were suspended due to opposition from Thailand, Cambodia and Vietnam. Laos responded by hiring the assistance of a Pöyry's subsidiary Pöyry Energy Ltd.

In June 2011, Pöyry estimated that Laos had given its neighbours sufficient opportunity to appraise and comment on the project through the Mekong River Commission, and so Laos and the Thai construction company, Ch. Karnchang, could proceed with the project. But the evaluation was subsequently revealed to be in violation of the 1995 Mekong Agreement and international law.

Later, Pöyry assessed the technical planning of the dam and issued a report on the impact the dam would have. Pöyry's report affirmed that the dam would be able to withstand natural disasters, and that it would not degrade water quality. The company recommended the use of fish friendly turbines and the construction of fish ladders. Though Pöyry admitted that there was not enough information on the dam's impact on fish stocks, ecosystems and the movement of sediments, it believed that with the help of further research and technical solutions construction of the dam could go ahead.

### PÖYRY'S UNCONVINCING REPORT

International Rivers (IR) analysed Pöyry's report and found it contained inconsistencies. The report failed to mention the numerous obligations of the MRC con-

cerning Xayaburi, which it fails to meet. For instance, Pöyry did not mention that a safe channel bypassing the dam should be created for up to 95% of major species of fish.

IR indicated that Pöyry has a conflict of interest concerning the dam. Pöyry and Ch. Karnchang are partners in a second dam construction project in Laos, Nam Ngum 2. It is likely that this was why the assessment concerning the Xayaburi dam was favourable, even though there are many factors against the project.

Thai energy authorities and commercial banks, in addition to the Laotian government and the construction company, have made use of Pöyry's report. Though Pöyry can claim that it only conducted a technical analysis, its repercussions could be profound. If the Xayaburi dam gets built, it is likely that a host of other dam constructions will follow suit on the mainstream of the river.

In October 2010 a strategic environmental assessment (SEA) funded by Finland was published on the combined impact of 11 dam construction proposals for the Mekong. It proposed that countries on the lower Mekong River should postpone decisions on hydropower dams on the mainstream of the river for at least a decade. The Mekong and its fish stocks are so crucial to tens of millions of people that the river should not be hastily harnessed for energy. ◀

TIMO KURONEN  
KEPA MEKONG

Xayaburi dam project has been given a Finnish bias



## CORPORATE ACCOUNTABILITY POLICY COUNTERS ACCOUNTABILITY DEFICIT

IT IS THE JOB OF GOVERNMENT TO SET GROUND RULES FOR CORPORATE BEHAVIOUR. IF THE STATE DOES NOT REGULATE CORPORATE ACTIVITY, IT WOULD BE LEFT TO CONSUMERS' PURCHASING DECISIONS OR SHAREHOLDERS TO DO SO.

► **THE POWER OF COUNTRIES TO REGULATE** corporate activity comes up against the fact that corporations have become bigger than many states. Countries compete with one another in the globalising world. Because their competitiveness hinges on that of their corporate sectors, companies and decision-makers often have common interests. Accountable corporate activity often gets characterised as a drag on competitiveness.

What complicates international regulation of corporate operations is the fact that global governance has not kept pace with globalisation. International conventions on human rights and ecological sustainability and their implementation lag behind.

The key challenge of regulation and transparency is also the magnitude of multinational companies and their chains of subsidiaries. The complex structure

of mega corporations, involving many subsidiaries and subcontractors, makes it hard even for upper management and shareholders to oversee operations.

Agreements and mechanisms on corporate accountability have been created at both national and international level. Improving their implementation and follow up could make corporate accountability succeed. This would improve the transparency of companies' operations by increasing their disclosure obligations concerning their impacts and value chains.

We need to see further progress at international level, as well as nationally in Finland. Corporate law concerning Finnish companies must be consistent with international guidelines. Finnish corporate accountability policy must strengthen and increase coherence between different ministries and policy areas. ◀

# CASE: TRADE UNIONS STRENGTHEN THEIR HOLD IN NICARAGUA'S FREE TRADE ZONES

## MULTI-STAKEHOLDER TRYOUTS IN FREE TRADE ZONES

► **FOR THE MOST** part Nicaragua's free trade zones contain foreign companies, which operate in tax-free conditions manufacturing products for export. Many foreign subcontractors also operate in the zones. There is much room for improvements in the conditions of workers in their factories, known as maquilas. Wages remain low and health at risk due to the use of chemicals and toxins.<sup>36</sup>

Many Nicaraguans are sceptical of discussion about corporate social responsibility (CSR). Research carried out in the country has found that there is scant knowledge of the notion of corporate accountability. Over 80 per cent of people polled consider CSR to be a marketing tool. People were baffled that companies receive certificates for the accountability of their activities, although their subcontractors maintain poor working conditions.

### IMPLEMENTING AGREEMENTS

The trade union Confederación Sindical de Trabajadores Josei Benito Escobar (CST-JBE) is active in improving the conditions of working conditions in factories in the free

Nicaraguans consider corporate accountability to be a marketing gimmick

economic zones.

CST-JBE has proposed that trade unions be represented in independent inspections of the maquilas, and that their results be made public.

CST-JBE has also managed to start up a tripartite committee comprising the union, the textile industry and government. Tripartite agreements have been signed, and they now need to be put into effect. Definite improvements in working conditions are still some way off. The union does not think that improving the situation should only be a voluntary option for the companies.◀

JOSÉ VALDIVIA  
KEPA NICARAGUA

36 CID and Kepa (2012)

## ENOUGH INTERNATIONAL NORMS

► **HERE ARE A NUMBER OF INTERNATIONAL CONVENTIONS** that regulate corporate activity. Compliance with them depends countries' political will and the discretion of corporations.

The most important of them, which companies should follow, is the UN Declaration of Human Rights, and its subsequent human rights agreements, environmental conventions and the ILO's conventions on workers' rights. The strongest agreements, however, are those made in the context of the World Trade Organisation (WTO). They also guide EU trade agreements. WTO agreements require that developing countries have investment friendly trade and investment policies. The majority of developing countries have liberalised their economies and reduced the obligations on investors, often at the expense of their citizens.

Recent decades have also seen the development of numerous international guidelines concerning corporate accountability in both the EU and OECD, as well as in the UN. In addition, many independent international bodies, such as the International Organisation for Standardisation (ISO), have developed standards

on social responsibility. Many of these guidelines are comprehensive and solid – there is no need to reinvent the wheel – but they do need to be consolidated, and their binding force, implementation and follow up increased. They should not contravene sanctions.

In particular, the OECD's guidelines for multinational enterprises are a comprehensive collection of recommendations on how corporate accountability should be carried out. The guidelines were first published in 1976, and they were updated for the fifth time in 2011. Altogether, 43 countries are committed to carrying out the guidelines and monitoring their application in corporate conduct.

The UN's principles on business and human rights (Protect, Respect, Remedy), drawn up by UN Special Representative John Ruggie in 2008, also guide the corporate sector, and the UN Human Rights Council is committed to carrying them out. Ruggie points out that the most usual barrier to accountable corporate conduct are the governance vacuums resulting from globalisation, where government does not have control over business activities. Also, in many countries existing laws are not enforced.



ISTOCKPHOTO

The cornerstones of Ruggie's framework are the responsibility of states to protect citizens from human rights abuses committed by third parties, the obligation of business to respect human rights, and guarantees of sufficient means of appeal for victims of human rights violations. Ruggie places the onus of responsibility on states. The European Commission has proposed that each country should create its own implementation plan for Ruggie's frames of reference.

### **DANGER OF GREENWASHING**

Within the UN framework there is UN Global Compact (UNGC), an initiative of Kofi Annan. This comprises 10 principles on human rights, labour, environment and anti-corruption.

The Global Compact is conceived as a moral compass for businesses. They can opt to commit themselves to these and pledge to report annually to how they carry them out. The initiative has come under fire from many quarters. Even the UN's own Joint Inspection Unit has reported that UNGC has no clear mandate, focus or influence. It has no criteria for joining, and there is no mo-

nitoring of participating businesses activities. Numerous enterprises have also failed to report to the UNGC with no consequence whatsoever.<sup>37</sup>

Many organisations have also accused the UNGC initiative of giving businesses an easy recourse to greenwashing of their irresponsible conduct using the Global Compact's logo. The UNGC secretariat has taken the criticisms on board and intends to terminate the participation of over 750 businesses, and tighten up the criteria for participating in it.<sup>38</sup>

The Global Compact has a Nordic network of which many Finnish businesses are members.<sup>39</sup> Some of them provide funding for the UNGC secretariat.<sup>40</sup> In its Development Policy Programme, Finland commits itself to supporting the UNGC.<sup>41</sup>

The UN Principles for Responsible Investment (UNPRI) has also been set up in the UN framework. By committing itself to the principles, a business has to take account of the quality of ecological, social and governance conditions of where it invests. Signing up to the principles is easy, and so far about a thousand businesses have joined in.<sup>42</sup>

In turn, the ISO has developed the ISO 26000 social

responsibility standards, based on the international agreements and guidelines we have looked at. Unlike other ISO standards, ISO 26000 cannot be used for certification, and instead functions as voluntary guidance for businesses.

In order to get rid of governance vacuums it would be important to promote the regulation of the corporate sector internationally. In its government programme,

the Finnish government commits itself to supporting efforts to enhance international norms and guidelines. For its part, the EU should reform all business legislation concerning European enterprises in the direction of greater accountability. In its corporate social responsibility strategy the European Commission sets the guidelines and principles mentioned above as the core set of international corporate accountability norms.<sup>43</sup> ◀

37 UN Joint Inspection Unit (2010)  
38 Confino (2012)  
39 Global Compact Network Nordic Countries  
40 Global Compact Foundation

41 MFA (2012)  
42 UNPRI  
43 European Commission (2011)

## WHY ISN'T VOLUNTARY ACTION ENOUGH?

The Extractive Industries Transparency Initiative (EITI), started in 2002, aims to increase transparency regarding profits in the mining and natural resource sectors. EITI's member states have to submit reports on the payments they receive from companies. These reports also have to be subject to auditing.

The problem with EITI is that natural resource rich countries have not joined it. Companies operating in them do not have to report payments they make, even if they are members of EITI. The most recent reporting for all countries belonging to EITI is for 2005.<sup>44</sup>

Mozambique is a good example of the problems with EITI. In 2009 the country joined the initiative and started to draw up its first report in 2010. The purpose of the report was to analyse figures for 2008. It contained figures for just six companies, and no grounds were given for excluding others. The report claims that only one per cent of Mozambique's budget was covered by revenue from the mining sector.

Civil society organisations demanded that information on mega investment agreements in the natural resource sector between the government and corporations be included in the report, but this remains secret. Mozambique was suspended from EITI for a little while, but has now been given a second chance. But the report now being made has come in for the same criticism as the first one, and relations between the country's EITI secretariat and civil society are bad.<sup>45</sup>

44 Publish What You Pay (2012)

45 Humberto Ossemame, development policy officer, Kapa Mozambique

## IS REPORTING A SOLUTION?

REPORTING HAS BECOME THE POLESTAR OF PROMOTING CORPORATE ACCOUNTABILITY. IT DOESN'T SOLVE EVERYTHING, BUT IT DOES INCREASE TRANSPARENCY AND OPENNESS. IT IS ALSO IMPORTANT THAT COMPANIES OPEN UP THEIR COUNTRY-SPECIFIC ACCOUNTS.

► **FUNCTIONING MARKETS** and democracy require openness concerning corporate conduct. The paucity of information is one of the main barriers to the public, consumers, investors, and those whose lives are affected by corporate activities being able to require companies to be responsible and be accountable. Reporting improves accountability as well as business competitiveness, access to capital and operational stability.<sup>46</sup>

Only about 120 Finnish companies and other organisations publish corporate accountability information.<sup>47</sup> This is a tiny fraction of Finland's more than 300,000 enterprises.<sup>48</sup> And yet CSR reporting is increasing exponentially. In 2010, over 4,000 European companies issued corporate accountability reports.<sup>49</sup> More companies recognise corporate accountability reporting as part of their strategic business operations, and not simply as a feature of corporate communications.

The most important reporting standards come from the Global Reporting Initiative (GRI), developed on the basis of broad corporate and civil society consultations. In addition to the GRI standards, there are also two US organisations and one created by the United Nations Environment Programme (UNEP), which nearly 4,000 organisations have joined. Further to standards that guide reporting, there are also international guidelines (see p. 17). In Finland the Government Ownership Steering Department has developed a standard under which state-owned or majority owned non-listed companies must submit reports in line with several different international guidelines.<sup>50</sup>

### CLARIFYING REPORTING PRACTICES THROUGH LEGISLATION

There are many problems with CSR reporting. Guidelines and reports are frequently complex and based on different standards. For stakeholders they lack crucial information, as human rights and environmental violations often go unreported. According to research on thousands of reports, they contain much irrelevant and erroneous information, deficient and unsubstantiated claims. A worst-case example was when a corporation made no mention in its reporting of emissions of a coal-fired power station belonging to it.<sup>51</sup> The main problem concerning reporting is the lack of monitoring mechanisms and sanctions.

Consequently, the civil society network European

Coalition for Corporate Justice is demanding that the EU uses legislation to clarify and standardise European corporate accountability reporting. The point is not to add to the reporting burden of company's, or to further complicate the confusion of guidelines. On the contrary, if there are clear and common rules, it will be possible to cut expenses and ensure equal treatment for all.

The OECD's guidelines and the UN's business and human rights principles could provide a basis for EU regulations, as they already apply to all EU countries. Legislation enforcement would be monitored and would face sanctions for non-compliance. Further, companies outside the EU with subsidiaries in Europe would report, for the sake of fairness, according to European legislation. The European Commission has a proposal for a directive on improving CSR reporting, and Finland should actively participate in the negotiations on it.

### SHEDDING DAYLIGHT ON COUNTRY-SPECIFIC FINANCIAL FIGURES

Corporate financial reporting also needs to be improved in addition of social accountability reporting. So-called country-by-country reporting could intervene in matters of tax evasion and avoidance. It could augment the scope for citizens, organisations and decision-makers to find out to which countries companies pay taxes and what kinds of tax agreements there are between countries and corporations. At the moment it is impossible to get hold of such information.

At present, the International Accounting Standards Board (IASB), comprising private sector accounting professionals, and registered in the US tax haven of Delaware, constructs accounting and financial reporting standards. IASB first published its standards in 2003, and they are statutory in the EU. IASB standards contain gaps, as a company can combine the results of subsidiaries in different countries into global or regional aggregates in such a way that it hardly reveals anything about the conglomerate's internal trading.<sup>52</sup>

In order to increase corporate revenue payment transparency, companies must be required to provide separate country-specific reporting on each country in which they operate. They must report country-specific income, profits, production volumes, taxation, investments, assets and debts. They must also list the names of their subsidiaries and sub-contractors. Country-by-country reporting



would elucidate the share of corporate internal trading, and provide information on where profits originate.<sup>53</sup>

Guidelines on corporate accountability reporting generally bypass taxation issues. GRI standards and OECD guidelines now include recommendations on this, and GRI favours publishing country-specific financial figures. Regrettably, many companies do not report this information.

Corporate accountability and country-by-country financial figures could be detailed in the same report. This would avoid additional administrative burdens for companies. But country-specific reporting should be done according to usual auditing procedures. There has been some recent progress on this. The European Commission had proposed requirements for country-by-country reporting by mining, gas, oil and forestry companies. There has been a similar initiative in the US. The details of these proposals are under negotiation. Finland has reservations about the Commission's proposal, contrary to the commitment of the government programme to promote country-by-country accounting. ◀

46 European Commission (2008) and KPMG (2011)

47 Finnish government (2011c)

48 Statistics for businesses for 2010 put the number at 318 951. Official Statistics of Finland (2011)

49 European Union Programme for Employment and Social Solidarity (2011)

50 Finnish government (2011c)

51 Jowit (2011)

52 Kepa (2009)

53 Christensen (2008)

## WHAT SHOULD BE REPORTED?

### ECONOMIC SUSTAINABILITY

Companies should report the impacts of their operations on different stakeholders. Apart from company owners, this should include workers and local communities. Country-by-country reports on financial figures are also part of reporting about economic sustainability.

### ECOLOGICAL SUSTAINABILITY

Companies should report the impacts of their operations on ecosystems, land, air, and water resources. Impacts describe such things as the materials, energy and water a company uses in its operations, plus the emissions and waste they cause.

### SOCIAL SUSTAINABILITY

Companies should report the social impacts of their operations. This category covers workers' rights, human rights, social accountability and product sustainability. Impacts on local communities are particularly important. Product sustainability includes consumer rights: health, safety and product information.

### GEOGRAPHICAL COVERAGE

Companies should report on the countries in which their subsidiaries and subcontractors operate. This would increase transparency about operations, and consumer protection.

Source: Mainly based on GRI's G3.1 reporting guidelines.

# CORPORATE ACCOUNTABILITY FOR DEVELOPMENT COOPERATION

IN RECENT YEARS THE PRIVATE SECTOR HAS GAINED A CENTRAL POSITION IN DEVELOPMENT POLICY. BUSINESS AID MUST TAKE ACCOUNT OF CORPORATE ACCOUNTABILITY AND THE INTERESTS OF LOCAL PEOPLE.

► **THE IMPORTANCE** of the private sector as a motor force for development has recently been underscored in Finland, in the EU and at the Busan High Level Forum on Aid Effectiveness. This shift is also evident in funding: the resources of the International Finance Corporation, the World Bank's private sector funding arm, has quadrupled over the last decade.<sup>54</sup>

The justification for corporate input for development cooperation resources is that investments significantly cut poverty, for instance by increasing employment and equality. Development cooperation in support of production targets the elimination of poverty and inequality, is ecologically sustainable and is based on respecting and promoting human rights.

But private sector projects supported by development cooperation funds don't always contribute to development policy aims. IFC projects, for instance, provide very little support for investments in low-income countries, and these projects are often not aligned with the development plans of the partner countries.<sup>55</sup>

## SCOPE FOR IMPROVEMENT IN FINLAND

In Finland, the private sector supports development cooperation funding, in particular with the assistance of Finnfund, Finnpartnership, concessional credit, and Aid for Trade projects. Others carrying out development projects include the employment and business administration side of the Geological Survey of Finland, the Technical Research Centre of Finland, the Finnish Funding Agency for Technology and Innovation, Finpro, the specialist network established by Finnish enterprises, and the state owned financing company Finnvera.

Finnfund is a development financing company that provides risk capital for profit-seeking projects in developing countries and Russia. Finnpartnership provides businesses with business partnership support and advisory services. Concessional credit projects constitute conditional Finnish development aid.

For over 20 years, the Finnish concessional credit scheme has sought to support economic and social development in the South by drawing on the knowhow of Finnish companies. The system serves today as an example of how not to do private sector development projects. Evaluations have shown it to be a poor instrument for development and cutting poverty. Weaknesses have been identified in the environmental and social sustain-

ability of its projects, and local communities are rarely involved in the projects or their planning.<sup>56</sup> The Foreign Ministry has finally decided to do away with the system and develop a new support instrument in its place. This must ensure corporate conduct that is accountable, ownership by partner countries, and positive development impacts.

Aid for Trade also supports the private sector. The aim of projects is to improve the scope for developing countries to translate the challenges of WTO trade and investment agreements into palpable benefits. Projects should promote accountability in business operations by providing support for local investment, the development of business legislation, and local business activity.

All support for businesses by development cooperation funds requires accountability according to national and international norms. Development cooperation must not support the tax haven economy. Decision-making concerning private sector support must be done with the agreement of all sides, including local communities. ◀

54 Eurodad (2010)

55 The Bretton Woods Project (2012)

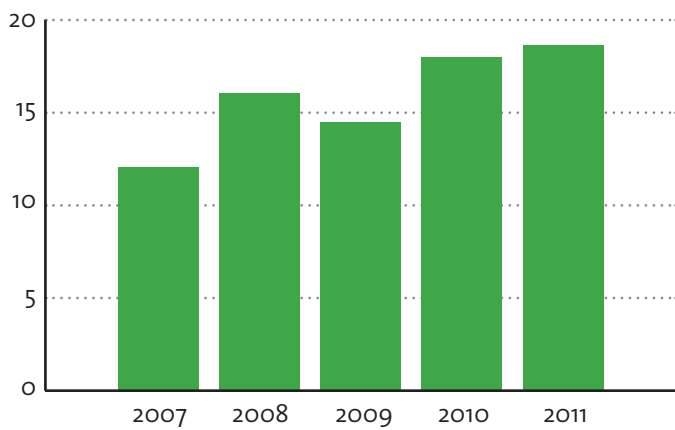
56 MFA (2012)

## FINFUND'S TAX HAVEN INVESTMENTS



Source: Finnfund, 2012

WORLD BANK SUPPORT THROUGH INTERNATIONAL FINANCE CORPORATION (IFC) FOR PRIVATE SECTOR IN 2007–2011 (Billion dollars)



Source: IFC (2011)



## A CIVIL SOCIETY ISSUE

CIVIL SOCIETY ORGANISATIONS PLAY AN IMPORTANT ROLE AS WATCHDOGS OF CORPORATE ACCOUNTABILITY OR AS PARTNERS TO ENTERPRISES.

► **CORPORATE ACCOUNTABILITY** decides the ability of companies to pay attention to their stakeholders and to ensure that they benefit as much as possible from business operations. Organisations and organised local communities can help companies to operate accountably. CSOs can channel valuable opinions to companies, and pick up on weak incoming signals.

Finnish CSOs that monitor corporate activities include Finnwatch, Fair Trade Finland, and Pro Ethical Trade Finland. But in many developing countries organisations find that advocacy related to corporate activities is dangerous. Companies and undemocratic governance often have identical interests, and questioning their behaviour can pose a threat. This is why reinforcing people's rights awareness and possibilities to have an influence is just as important as developing infrastructure and technology.

Many CSOs are also interested in working with businesses in running different sorts of programmes and projects. When a company enjoys the support of CSOs, it may be easier for a company to make investments whose target group is the poorest sections of the population. The functional and financial support some CSOs get from businesses may also be important for them. Collaboration between companies and CSOs can prove fruitful as long as the former don't have greenwashing as their ulterior motive. It is also important that the baselines, principles and values of the CSO and the business correspond. ◀

### COMMUNITY PUTS AN END TO FORESTRY FIRM'S ABUSES

Chikweti Forests established a large forest plantation in Niassa, northern Mozambique, with funding from the Swedish-based Global Solidarity Forest Fund. GSFF is a forestry sector investment fund, which, in addition to generating profits, aims to support local community development and the environment.

The Niassa project sought to afforest treeless areas. But this is not what happened. Trees were cut down to make way for the planting, and local communities were relocated. This reduced scope for local population to farm the land. The situation culminated in violent clashes, after which the Provincial Farmers Union (UPC) took up the issue together with the locals. Efforts for a negotiated settlement between the forestry company and the local government failed.

The National Farmers Union (UNAC) attracted international attention to the case through its network of contacts. This prompted media interest and details of the case spread to the home turf of GSFF's partners. In the end the Mozambican government joined those calling for an end to the abuses at Niassa. The local union appealed directly to GSFF's stakeholders to question why they were investing in projects that deprived the poorest of the poor.

As a result of the appeal, GSFF sent a delegation of stakeholders to make an on-site investigation of the situation. This reported that the project did not meet the principles of investment accountability. The land acquisitions were halted. Local farmers continue to prepare for future struggles by such things as becoming proficient in land and environmental legislation.

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