

Ethics in the Financial Sector: At Home and Abroad

Remarks by Jim McArdle to EthicsCentre CA, Toronto, Sept. 28, 2010

First, I'd like to thank you for the opportunity to join you today to speak on Ethics, especially to such a knowledgeable group. Second, congratulations to Gail Henderson. I'm sure you've been following the work of Dr. John Ruggie at the U.N. Good luck.

As you heard, part of my role at EDC is as the executive responsible for Corporate Social Responsibility (CSR). I have been involved with CSR for many years, first as a transaction lawyer on financing of projects, now as an executive at the policy level--playing a role in the final decision on tough situations.

EDC has witnessed companies around the globe sustaining their success by doing business ethically and responsibly. We also *all* have seen breakdowns in ethics—think Enron, Worldcom, Siemens. It's tough to put boundaries around ethics.

That's why ethics is a moving target--not only because of higher expectations of our publics at home, but also different cultural perceptions abroad. Many Canadian companies are surprised when they venture abroad.

In my remarks today:

- I'll tell you a little about EDC and our own ethics program.
- I'll give you a sense of the ethical and reputational dilemmas a financial institution faces, primarily in the international arena—our field of expertise. With respect to the environment, our role has become much clearer through guidelines and standards, such as the IFC Performance Standards, Environmental Policies and OECD Common approaches, which I will outline as well.
- I will also touch on how these dilemmas have shaped the evolution of ethics at EDC. Mainly, I'll do this through real situations we have faced.

First let me give you a brief overview of EDC:

EDC is Canada's export credit agency (ECA), in business for 66 years. Our mandate is to help Canadian companies develop and expand their exports and investments abroad.

A Crown corporation, EDC operates at arm's length from the government. EDC is financially self-sufficient and works like a commercial bank, providing loans and insurance. Most of our focus is on "projects", but ethics touches a much wider spectrum.

Many other countries have an ECA similar to EDC; each seeks to promote its own country's exports. This could lead ECAs to try to tip the balance in favour of their exporters, by using uncompetitive or unfair advantages.

Fortunately, there are agreements through the Organization for Economic Cooperation and Development (OECD) to ensure a level playing field by ECAs. For example, there are agreements on price-setting, premiums and interest rates.

These arrangements expanded to other areas in the late 1990s, notably the environment and anti-corruption, leading to:

- the *Common Approaches on the Environment*; and
- *an Action Statement on Bribery*.

Over the past 12 years, EDC has developed strong CSR policies and practices to comply with both domestic and international laws and standards—which have also been reinforced throughout this period. Today, CSR is fully integrated into our internal culture and operations.

Code of Conduct

Starting with a policy on basic ethics, in the late 1990s, we created our *Code of Business Ethics and Code of Conduct*.

We're proud that EDC was the first Crown to introduce a formal *Code of Conduct*. It applies to all Board members, senior management and employees. The Code of Business Ethics covers issues including ethical conduct, conflicts of interest, bribery and corruption, transparency and confidentiality, environment and human rights. We have a yearly sign-off and refresher program.

The Code also represents the first time the Board formally became involved in CSR issues. A few years later, in 2000, we presented to the Board the concept of CSR as one of our operating principles, integrated into our business.

Since then these principles have evolved in many ways. In short:

- We developed an Environmental Review Directive (ERD) and Environmental Policy.
- We created a dedicated Environmental Advisory Service to do environmental risk assessments.
- We developed a Disclosure Policy and process to ensure transparency about projects we plan to support.
- We led discussions in recent years with diverse parties involved in extractive projects in challenging markets on how to engage local communities.
- Most recently, we added a Human Rights Statement and expanded the role of our Political Risk Assessment Department to also assess Human Rights issues.

- All new measures continue to be reviewed by our Board of Directors.

Let me return to our topic of ethics—particularly the risk of bribery and corruption in global trade—and look at real cases where we had to apply our policies and practices.

As I mentioned, EDC signed onto the OECD Action Statement on Bribery in 1999. Shortly after, this was reinforced in Canada by the *Corruption of Foreign Public Officials Act*, making it a criminally-indictable offence to bribe foreign public officials.

This legislation was motivated by the view that bribery hinders both economic and political progress. It decreases the quality of goods and services, discourages fair competition and impedes economic development.

EDC's own anti-corruption program takes a three-pronged approach:

- It builds awareness of the issues to employees and customers, through our Code, letters to clients, speeches and articles, and in direct discussions with Canadian companies.
- Underwriters work with our Corporate Responsibility and Political & Human Rights Risk Assessment teams to identify potential corrupt practices in their transaction analysis.
- We require customers who use our financial services to sign a declaration that they are not or will not be involved in bribery and corruption. This means EDC has the right to terminate policies and refuse claim payments if a customer is found to engage in bribery or other corrupt practices.

Case Studies: Bribery & Corruption Issues

As it happens, shortly after we signed on to the Action Statement on Bribery, one of our clients was charged with bribery in an African country.

We weren't supporting that particular project, but did that mean we shouldn't support any project or exports this company undertook?

How far did our responsibility go? Were allegations and charges enough for us to withdraw support?

We waited. We debated. Charges turned into a conviction in the country of operation. The World Bank refused to support the company.

Solution:

We temporarily suspended our support to the company. During this time, we worked intensively with the company to help it understand our expectations before we could resume support.

We returned to supporting the exporter after it developed a comprehensive remediation program aimed at the detection and deterrence of bribery and corruption in its business. We continued to monitor the company's progress for a number of years.

A Canadian company seeking our support is facing allegations of corruption in the form of influence-peddling in Canada.

There were unsubstantiated allegations of corruption and investigations by Canadian authorities, but to date, no charges have been laid. The allegations largely related to the exporter's joint venture partner.

Solution:

We conducted enhanced due diligence around the Canadian company. We worked with the company to provide guidance on improving its ethics practices. For example, we helped it put in place measures such as a *Code of Business Ethics*, and developing staff training. We continue to monitor its progress.

A payment dispute arose over alleged bribery payments expected from a Canadian exporter.

An approach was allegedly made to the Canadian exporter by his potential foreign buyer, a state oil company official, that if he were to pay a bribe, his supply contract would be approved for payment.

Solution:

We suspended support for more than a year to probe the company's operations. Besides reviewing the policies of the foreign oil company, we held a number of conversations with it to understand their anti-corruption practices, how it implements them and how effective that implementation was.

We eventually were able to get comfortable with its processes, but all transactions with the entity are given close scrutiny for any red flags of potential bribery.

A major Canadian exporter has an opportunity to sell equipment to a private foreign airline.

The owner of the airline is a prominent local businessman under investigation in his country by anti-corruption authorities for making inappropriate contributions to political campaigns. The country ranks in the bottom quartile of Transparency International's Corruption Perceptions Index, indicating a high risk of corruption in business transactions.

As well, the equipment sale is through a sole-source contract. In such arrangements, the opportunity for payments is higher.

Solution:

EDC looked into the transaction, including making a field visit to the company. While there is no indication of inappropriate payments in the deal EDC is being asked to support, we have had a number of conversations with the foreign airline to understand its practices, to detect and deter corruption and to convey what we feel are best practices in the area. The deal has not concluded for other reasons.

Traditionally, most people think of ethics as conflicts of interest or bribery and corruption. However, this view of ethics is evolving and becoming much broader.

Most recently, the OECD has started to focus on human rights. EDC is working with Dr. John Ruggie, UN Special Representative for Business and Human Rights, to help develop a human rights assessment process for transactions.

This extends the concept of ethics to moral issues and poses new challenges, for example, what is the role of a financial institution in applying Canadian values to other cultures?

Human Rights Issues

EDC financing was requested to support the sale of transportation equipment to the national police force in a foreign country.

We were concerned the transportation equipment would not just be used for transporting equipment, but also for re-settling the local population at a mine site.

The country has a mixed human rights record, including a poor track record on re-settlement. On the other hand, for the Canadian exporter, the sale would enable the company to maintain jobs in Canada.

Solution:

EDC recognized we could not control the use of the equipment. What we did know is that the country's record of past abuses was clear. We concluded that it was reasonably likely that receipt of this equipment would exacerbate an existing human rights problem. We declined support.

EDC was asked to finance the sale of surveillance equipment to a foreign government.

The equipment would be used by security forces, which were poorly governed. The security personnel had also been implicated in the politically-motivated massacre of civilians. In addition, it was unclear *how* or *if* access to the surveillance equipment or video footage from it would be controlled.

The Canadian exporter needed our support, because the company was up against other foreign companies also bidding on the contract, with possible support from their own export credit agencies.

Solution:

Once again, EDC recognized we could not control the use of the equipment or video footage. The security forces' record of past mismanagement and abuses was clear. It was reasonably likely that receipt of this equipment would exacerbate an existing human rights problem. We declined support.

EDC was asked to provide financing to a Colombia oil & gas company in support of Canadian exports.

The Company operates in areas of conflict and entered into security arrangements with the Colombian army. These factors exposed it to allegations of worsening the human rights situation in Colombia.

Solution:

We met with the company to understand what it was doing to manage human rights risk. The company clarified how it integrates human rights risk management into all its CSR policies and practices.

We were convinced that the company is proactively managing the human rights risk within the country context. EDC agreed to provide financing.

As a counter-example, EDC was also asked to lend to a Canadian extractive company in support of its operations in Colombia.

Again, the company operates in areas of conflict in Colombia and had entered into security arrangements with the Colombian army. These factors exposed it to allegations of worsening the human rights situation in Colombia.

Solution:

EDC also met the company to understand what it was doing to manage its human rights risk. We believed the company had not integrated human rights risk management into its CSR policies and practices at a level we would have anticipated, given the risk issues to which it was exposed.

We declined support. However, we are still working with company to see if it can increase its ability to proactively manage the human rights risk within the Colombian context.

Other “Moral” Issues

Our credit insurance services were requested for the sale of equipment to a legal, foreign gambling operation.

The foreign owners faced allegations of racketeering.

Solution:

We examined the transaction for indicators of improper conduct and corruption. For example, we examined the casino for its commitments to responsible gambling operations.

We could not find any clear evidence to support the allegations. We provided insurance to the Canadian exporter.

We also had a request for credit insurance related to sales in the adult entertainment industry.

The Canadian exporter provides digitally mastering DVDs containing hard-core pornography, which is a legal product in Canada and the exporter operates legally here.

However, we had no knowledge of where the material would be sold, how the films would be made and sold in foreign markets; for example, would there be a risk of underage actors or other abusive and illegal practices in those markets?

Solution:

We concluded the product could be ethically unacceptable in some cases and markets. EDC declined support.

Likewise, we have faced challenges related to support for tobacco products, nuclear power, weapons and hazardous products such as asbestos. Each case must be reviewed on own merits, within Canadian and international laws and standards.

Today, too, we even need to look at the kind of customer with whom we are dealing.

The Government of Canada's Directive on Persons of Integrity is a recent directive to financial Crown corporations that reflects requirements by commercial banks to “*know their customer.*” Basically, it places the onus on Crowns like EDC to understand the individual business owners to whom we provide services, to ensure we are not supporting people whose backgrounds might raise concern with the Canadian public.

As you can see, the goal-posts keep changing in the field of CSR and ethics. As new situations and standards evolve, greater due diligence is also required. This always has the potential to hamper EDC's ability to expand Canadian exports and investments—our true mandate.

Neither is our role to police the ethics of every business, or the values of every country. At the same time, we are expected by the Canadian public, our taxpayers, to behave ethically and support responsible business and trade.

We need to find a balance between ensuring our own house is in order and helping customers mitigate *their* trade risks by helping them do business responsibly. This is more important than ever as Canadian trade and investment becomes more international and transactions more complex.

To summarize, let me reiterate how we try to find the right balance:

- EDC follows a well-established internal *Code of Ethics and Conduct*, and international standards and guidelines.
- We have our own staff of specialists in areas of environmental, political and human rights risk assessment.

- We engage the diverse expertise and perspectives of our Board members.
- We regularly convene a CSR Advisory Council – a group of nine eminent Canadians who meet semi-annually to provide advice to EDC’s senior management on general CSR practices. Ethical issues regularly enter into our discussions.
- We do reputation risk assessments, basically an ethics check, of projects we consider supporting; we generally have our financial officers do the screening for non-project transactions.
- We disclose the projects we are planning to support on our website, enabling questions and comments from the public.
- We work with international experts like Dr. Ruggie to ensure we are applying the latest thinking on the subject.

I welcome your questions. I also invite you to comment on some of the sticky ethical situations you may be facing, and how your own policies and practices help you respond to them.

Thank you.